IV

Omit from page 22, beginning with the words "single acknowledgment", through and including page 24, and insert the following in lieu thereof:

"Acknowledgments and recording data omitted because immaterial."

V

Omit all of Plaintiffs' Exhibit 3, beginning on page 25 and extending to page 34, and insert the following:

"This Exhibit was an oil and gas lease from J. C. Barrett to
3 J. A. Reynolds, dated August 26, 1929, and, except as to parties and descriptions, is identical with Exhibit 2 and is therefore omitted."

VI

Omit all of Plaintiffs' Exhibit 4, beginning on page 34 and extending down to the phrase "the witness" on page 44, and insert in lieu thereof the following:

"This Exhibit was an oil and gas lease from J. J. Fuller and wife to Mamie S. Hammonds, dated September 22, 1930, and, except for parties and descriptions, is identical with Plaintiffs' Exhibit 2, and is therefore omitted in printing."

VII

Omit all of page 49 and that portion of page 50 down to the words "Plaintiffs' Exhibit 5–b", and insert the following in lieu thereof:

"Acknowledgments and recording data omitted because immaterial."

VIII

Omit all of page 54 and down to the phrase "The witness" on page 55, and insert in lieu thereof the following:

"Acknowledgments and recording data omitted because immaterial."

IX

Omit from page 65 beginning with the words "W. P. Luse" through page 67, and insert in lieu thereof the following:

"Division of royalty interest omitted because immaterial."

4 X

Omit from the top of page 70 down to the words "Plaintiffs' Exhibit 6–b" at the bottom thereof, and insert in lieu thereof the following:

"Detailed description omitted because immaterial."

XI

Omit from page 76 beginning with the words "Being a part of the Jackson Couch Survey" down to the phrase, on page 77 beginning "it is understood and agreed, etc.", and insert in lieu thereof the following:

"Detailed description omitted because immaterial."

XII

Omit from the close of the phrase, on page 99, beginning "In testimony whereof witness our hands this the _____ day of October, A. D. 1933", down to the phrase, on page 102, "The witness" and insert in lieu thereof the following:

"Acknowledgments and recording data omitted because immaterial."

XIII

Omit from the top of page 162 down to the phrase, on page 164, beginning "statement attached to the claims for refund, etc.", and insert in lieu thereof the following:

5 "Omitted because identical with Plaintiffs' Exhibit A."

XIV

Omit from page 168 beginning with the words "State of Texas, County of Gregg" down to the word "claim" on page 174, and insert in lieu thereof the following:

"Omitted because identical with Plaintiffs' Exhibit 1."

Executed July 31, 1936.

Staley Building, Wichita Falls, Texas.

HARRY C. WEEKS,
Attorney for Appellants, J. J. Perkins and Mrs. Lois Perkins.
CLYDE O. EASTUS,
J. G. B.,
FRANK B. POTTER,
J. G. B.,
J. L. BACKSTROM,
Attorneys for Appellee, W. A. Thomas, Collector of Internal Revenue.

6 In United States District Court, Northern District of Texas

[Caption omitted.]

No. 4843—At Law

J. J. PERKINS AND WIFE, MRS. LOIS PERKINS

vs.

W. A. THOMAS, COLLECTOR OF INTERNAL REVENUE

First amended original petition

Filed May 23, 1936

To the Honorable Wm. Hawley Atwell, Judge of the District Court of the United States for the Northern District of Texas:

Now come J. J. Perkins and Mrs. Lois Perkins, the plaintiffs in the above styled and numbered cause, and leave of the Court being first had and obtained, file this their First Amended Original Petition, in lieu of their Original Petition filed herein on December 28, 1935, and for such amended petition plead as follows:

I

7 Now come J. J. Perkins and Mrs. Lois Perkins, who will be hereinafter styled plaintiffs, complaining of W. A. Thomas, Collector of Internal Revenue, who will be hereinafter styled defendant, and respectfully allege:

II

The plaintiffs, J. J. Perkins and Mrs. Lois Perkins, are now, and were at all times hereinafter referred to, husband and wife. They, and each of them, are citizens of the United States and reside in Wichita Falls, Wichita County, Texas, which is within the Northern District of Texas. The defendant, W. A. Thomas, is now, and was at all of the times hereinafter referred to, the duly appointed, qualified and acting Collector of Internal Revenue for the Second Collection District of Texas. His office, as well as his place of residence, is in Dallas, Dallas County, Texas, which is within the Northern District of Texas. All of the acts and conduct of the said W. A. Thomas hereinafter complained of were done and performed in his official capacity as such Collector.

III

This suit arises under the Constitution and Laws of the United States, in that it is a suit brought to recover federal income taxes collected by the defendant from the plaintiffs under and by force of the Laws of the United States.

IV

Plaintiffs show to the Court that throughout the year 1933, as well as for many years prior thereto, they lived together as husband and wife in Wichita Falls, Texas, and during that year they owned various properties which constituted their community property under the laws of Texas, and received from said property, and from
8 other sources, income which was their community property under the laws of Texas, so that, by virtue of the provisions of the Revenue Act of 1932, they were required to file income tax returns and to pay income taxes to the United States of America. These income tax returns were filed for the year 1933 upon a basis of the calendar year 1933, and upon the basis of cash receipts and disbursements. Each of the plaintiffs filed a separate tax return and therein reported a total net income, subject to taxation, of $75,078.58; one half of which was reported by the Plaintiff, J. J. Perkins, as his share of the community income, and the other one-half of which was reported by the plaintiff, Mrs. Lois Perkins, as her share of the community property and income. Thereafter, and in due course, the plaintiffs paid in installments to the defendant the amount of taxes shown to be due by their respective returns; the dates and amounts of such payments being as follows;

By the Plaintiff, J. J. Perkins:	
March 14, 1934	$25.00
April 12, 1934	742.47
June 13, 1934	792.60
September 12, 1934	755.04
December 12, 1934	755.03
Total	$3,070.14
By the Plaintiff, Mrs. Lois Perkins:	
March 14, 1934	$25.00
April 12, 1934	750.47
June 13, 1934	800.60
September 12, 1934	763.04
December 14, 1934	763.03
Total	$3,102.15

These returns and payments were made by the plaintiffs, and
9 each of them, in a faithful and bona fide effort to comply with the law fixing their income tax liability for said year and to discharge the liabilities so fixed.

V

Thereafter, the books and records of the plaintiffs were audited by representatives of the Bureau of Internal Revenue to determine the accuracy and correctness of said returns, and, based upon this examination, the Commissioner of Internal Revenue determined and fixed the total net community income of the plaintiffs as $93,588.22, and the equal share of the same, upon which each of the plaintiffs was taxable at $46,794.11. Based upon this determination

he made an assessment of additional income taxes for the year 1933 against the plaintiffs, and each of them; the amount of additional taxes assessed against each being $1,316.37. Plaintiffs say that said additional assessments were made on or about October 24, 1935. Thereafter, and in due course, said assessments were certified by the Commissioner of Internal Revenue to the defendant Collector at Dallas for enforcement and collection, and the plaintiffs paid the defendant Collector, on or about October 24, 1935, the additional tax so assessed, together with interest thereon; the interest collected from each of the plaintiffs at said time amounting to $125.70.

VI

Plaintiffs further say that the additional tax so assessed and collected from the plaintiffs, and each of them, was erroneous, illegal, and excessive, in that it was based upon items of alleged income which were not, under the Revenue Act of 1932, taxable to the plaintiffs, or either of them, and upon the disallowance of deductions from gross income to which the plaintiffs, and each of them, were entitled under the Revenue Act of 1932, all of which is more fully shown by the facts hereinafter alleged.

10 VII

(a) In the year 1933, the plaintiffs owned as their community property a 3/8ths share in a certain interest in oil and gas leaseholds on lands in Gregg and Upshur Counties, Texas. Certain of these interests had been acquired by plaintiffs through the Faith Oil Corporation and under and through an assignment thereof made to Faith Oil Corporation on or about July 24, 1931. There is attached hereto and marked Exhibit "A" a copy of said assignment, which is true and correct in each and every detail, save and except that the detailed description of the lands covered is omitted as immaterial. Said exhibit is hereby made a part hereof for all purposes. By virtue of the terms of said assignment, one fourth of all of the oil to be produced from said property was to go to the assignors in said instrument until they had received oil of the value of $395,000.00. Such rights to oil to be produced under oil and gas leases are usually referred to and known to those engaged in the business of producing oil as an "oil payment."

(b) In addition to the interests so acquired, the plaintiffs likewise owned and held, in 1933, an undivided 3/8ths interest in a certain oil and gas lease on lands in Upshur County, Texas, acquired with Faith Oil Corporation and W. J. Green under an oil and gas lease executed by E. H. Brawley and wife to W. J. Green, which oil and gas lease provided, in addition to the cash consideration that the lessors should receive 1/4th of 7/8ths of all of the oil to be produced therefrom until they had received oil of the value of approximately $45,000.00.

(c) The plaintiffs held, as above stated, under said assignments and leases throughout the year 1933, an undivided 3/8ths interest in such rights as were conveyed thereby and participated in
11 the operation of said properties for oil and gas throughout the year. There was produced throughout said year oil in sufficient quantities to that, on account of that portion of said oil payments respectively applicable to the 3/8ths interests of the plaintiffs, the holders of said oil payments received oil of the value of $9,614.52. In the determination of the plaintiffs' net income and alleged additional tax liability for the year 1933, made by the Commissioner of Internal Revenue heretofore set forth, that official treated said sum of $9,614.52 as a part of the gross income of plaintiffs and thereby increased their community income by said sum of, to-wit, $9,614.52.

VIII

Plaintiffs say that no part of the oil which went to the aforesaid assignors to apply upon said oil payment was, or had ever been, the property of the plaintiffs. On the contrary, that portion of said oil was, when produced and sold, the property of the said assignors or lessors, and said oil, as it was produced, was placed in tanks upon the various tracts from which it was produced for the account, and for the use and benefit, of said assignors or lessors and was thereafter run from said lease storage tanks into various oil pipe lines to the credit of said assignors, or lessors, and was sold by them when and as they saw fit and under such terms and conditions as they saw fit, and payment therefor was made directly to said assignors or lessors. All of this was in accordance with a well established trade practice and custom by which, in the case of such oil payments, the holder thereof is considered, deemed, and treated by all of those dealing with such oil and gas leases, or the oil produced therefrom, as the owner of a fractional portion of the oil in and under the leased premises and produced therefrom, and as
12 entitled to receive the oil in kind and dispose of same. Because of these facts, the aforesaid increase in the community income of the plaintiffs, and each of them, was erroneous and illegal.

IX

Plaintiffs would next show to the Court that in the year 1924, they acquired, as their community property, an undivided one third (1/3) interest in certain lands in Moore County, Texas, known as the Ozier Ranch, embracing approximately 5,400 acres. The plaintiffs acquired the aforesaid interest in and to the fee simple title to said lands. Record title, in accordance with a contract, was acquired in 1925. Both in 1924 and 1925, the principal value of said lands was their prospective and potential value for the production of oil or gas, and at said times it was considered by all of those informed as to the possibilities and probabilities of producing oil or gas in this area of Texas that said lands, or a substantial portion

thereof, would produce oil or gas in paying quantities, and, but for the value attributable to and attaching to said lands on account of the fact that the same would probably produce oil or gas, and but for the then market value of the minerals in and under said land, the plaintiffs would not have purchased or acquired any part or interest therein. The plaintiffs paid for said interest the sum of $10,000.00 and plaintiffs say that at least 3/4ths of said purchase price represented and was the cost of the oil, gas, and mineral content of said land. In the year 1933, the taxpayers sold and conveyed all of their interest in the oil, gas, and other minerals in and under said land and received therefor $31,073.33. In their said income tax returns for the year 1933 they reported this sum as the gross receipts from said sale, and in fixing and reporting the profit therefrom deducted as the cost of the mineral interest so sold the sum of $7,500.00, which was, as plaintiffs allege
13 and believe, the portion of the cost of said undivided one third interest in said lands attributable to and properly allocatable to the minerals so sold and conveyed.

X

In determining the plaintiffs' community income for the year 1933, the Commissioner of Internal Revenue disallowed said deduction of $7,500.00, and treated the total sale price of $31,073.33 as income from said sale taxable to the plaintiffs, thereby increasing their community income by the sum of $7,500.00.

XI

Plaintiffs say that in determining the taxable income and gain from said sale, they are, under and by virtue of the Revenue Act of 1932, entitled to deduct from the selling price of said property the cost thereof, and that the acts and conduct of the Commissioner of Internal Revenue in so increasing their taxable net income were erroneous and illegal.

XII

Plaintiffs say that because of these facts, they are entitled to have and recover of and from the defendant so much of the income taxes and interest paid by them to the defendant, as heretofore set forth, as is attributable to the two items heretofore referred to, and plaintiffs say, upon information and belief, that all of the tax and interest paid to the defendant, Thomas, on or about October 24, 1935, is attributable to the aforesaid errors.

XIII

Plaintiffs further show to the Court that on or about
14 November 8, 1935, they, and each of them, filed with the defendant Collector written claims for the refunding of such taxes and interest; said claims, and each of them, being based upon

the same facts and claims as are herein set forth. Thereafter, said claims, and each of them, were considered by the Commissioner of Internal Revenue, and, on or about December 16, 1935, each of said claims was rejected and disallowed by the Commissioner of Internal Revenue.

XIV

Plaintiffs further say that all of the acts and conduct of the defendant herein complained of were done by him in his official capacity as Collector of Internal Revenue and under instructions from his superior officers, and that on this account, the said defendant is entitled to a Certificate of Probable Cause for his said acts.

Wherefore, premises considered, plaintiffs sue, pray for service to defendant, and that, upon final hearing hereof, they have judgment against defendant for the taxes and interest so collected from them on October 24, 1935, together with interest from the date of payment as provided by law, and all costs of suit; and that the defendant be awarded a Certificate of Probable Cause; and that the plaintiffs have such other and further relief, special and general, as they may be entitled to receive under the facts alleged.

(Signed) HARRY C. WEEKS,
WEEKS AND MORROW,
Attorneys for Plaintiffs.

Staley Building, Wichita Falls, Texas.

EXHIBIT A—Omitted because identical with Plaintiffs' Exhibit No. 1 shown elsewhere in the record, as per stipulation of counsel copied at page one hereof.

* * * * * * *

In United States District Court

Defendant's answer to first amended petition

Filed June 9, 1936

Now comes W. A. Thomas, Collector of Internal Revenue, defendant in the above entitled and numbered cause, by and through Clyde O. Eastus, United States Attorney for the Northern District of Texas, and demurs generally to plaintiffs' cause of action and says the same is insufficient in law to entitle plaintiffs to judgment, and of this he prays the judgment of the Court.

(S.) CLYDE O. EASTUS,
United States Attorney,
(S.) FRANK B. POTTER,
Assistant United States Attorney,
(S.) J. L. BACKSTROM,
Special Attorney,
Treasury Department.

Defendant denies all and singular the material allegations in plaintiffs' petition contained, except those hereinafter specially admitted, and says the same are untrue, and demands strict proof thereof, and of this he puts himself upon the country.

(S.) CLYDE O. EASTUS,
United States Attorney,
(S.) FRANK B. POTTER,
Assistant United States Attorney,
(S.) J. L. BACKSTROM,
Special Attorney,
Treasury Department.

16 Answering further herein, if further answer be deemed necessary, defendant denies and alleges as follows:

I

Defendant admits the allegations contained in Paragraph II of plaintiffs' first amended petition.

II

Defendant admits the allegations contained in Paragraph II of plaintiffs' first amended petition.

III

Defendant admits the allegations contained in Paragraph III of plaintiffs' first amended petition.

IV

(a) Defendant admits the allegations contained in Paragraph IV (a) of plaintiffs' first amended petition.

(b) Defendant denies the allegations contained in Paragraph IV (b) of plaintiffs' first amended petition.

V

Defendant admits the allegations contained in Paragraph V of the first amended petition except that it is alleged that the additional taxes assessed against the plaintiffs of $1,316.37 for the calendar year 1933 were assessed on October 15, 1935, and that the plaintiffs paid said tax and interest on October 25, 1935.

VI

Defendant denies each and every allegation contained in Paragraph VI of plaintiffs' first amended petition.

17

VII

Defendant admits the allegations contained in Paragraph VII of the first amended petition, but denies that any claim for refund has been filed on account of any tax paid by the plaintiffs relative to the income in controversy derived from the lands in Upshur County, Texas, as alleged in said Paragraph VII, subdivisions (a), (b), and (c), and denies that by virtue of the terms of the Assignment, attached to the petition and marked Exhibit A, one-fourth of all the oil to be produced from said property was to go to the assignors until they had received oil of the value of $395,000.00 and also denies the similar allegations in Paragraph VII (b) as to the Upshur County lease.

VIII

Defendant denies each and every allegation contained in Paragraph VIII of plaintiffs' first amended petition.

IX

Defendants admits that the plaintiffs, in the year 1924, acquired as their community property an undivided interest in and to the fee simple title to certain lands in Moore County, Texas, known as the Ozier Ranch, embracing approximately 5,400 acres. Defendant denies that the principal value of said lands was their prospective and potential value for the production of oil or gas in this area or on said lands at that time. Defendant denies that plaintiffs would not have purchased any interest in said lands were it not for the possibility of oil or gas production. Defendant admits that the plaintiffs paid for said interest in said lands in 1924 the sum of $10,000.00. Defendant denies that at least three-fourths of said purchase

18 price represented and was the cost of the oil and gas and mineral contents of said land, and expressly alleges that no part of said purchase price represented or was the cost of any oil, gas, or mineral contents in said land. Defendant admits that in 1933 the plaintiffs sold and conveyed all of their interest in the oil, gas, and other minerals under said land for a price of $31,073.33 received by them. Defendant admits that the plaintiffs reported the said purchase price of $31,073.33 in their schedule of Item 30 in their income tax return for the calendar year of 1933 in computing their capital net gain and admits that they deducted from the capital gain so reported the sum of $7,500.00 as the alleged cost of their interest in said lands, attributable and allocable to the minerals so sold and conveyed.

X

Defendant admits the allegations contained in Paragraph X of plaintiffs' first amended petition.

XI

Defendant denies each and every allegation of Paragraph XI of plaintiffs' first amended petition.

XII

Defendant denies each and every allegation of Paragraph XII plaintiffs' first amended petition.

XIII

Defendant denies that the plaintiffs on or about November 8, 1935, filed with the defendant written claims for the refunding of taxes and interest based upon the same facts and claims as alleged in the first amended petition. The defendant admits that on or
19 about November 8, 1935, plaintiffs filed with the defendant written claims for the refunding of additional taxes paid by them for the year 1933 based upon some of the facts alleged in the first amended petition, but denies that said claims for refund are based upon the facts and contentions relative to the income derived from certain oil and gas leases on lands in Upshur County, Texas, as alleged in Paragraph VII of said first amended petition. The defendant admits that said claims and each of them were considered by the Commissioner of Internal Revenue and were on or about December 6, 1935, rejected and disallowed by the Commissioner of Internal Revenue.

XIV

Defendant admits that all of the acts and conduct of defendant herein were done by him in his official capacity as Collector of Internal Revenue for the Second Collection District of Texas, and under instructions from his superior officers, and that on this act the said defendant is entitled to a "Certificate of probable cause for his said acts."

XV

In the alternative, defendant says in the event it is held that said amount of $9,614.52 of so-called oil payments should not be included in plaintiffs' taxable income, defendant submits that the depletion allowed by the Commissioner of Internal Revenue as a deduction on account of said so-called oil payments should not be allowed. In the determination of plaintiffs' tax for 1933, the Commissioner of Internal Revenue allowed depletion in the amount of $2,919.16 on account of including said amount of $9,614.52 in plaintiffs' taxable income and, therefore, if said amount of $9,614.52 is eliminated from taxable income, the said amount of $2,919.16 allowed as depletion in respect thereof should be disallowed as a deduction in the determination of any refund found by the Court.

20 XVI

In the alternative, defendant further alleges, in the event it is held that said amount of $9,614.52 of so-called oil payments should not be included in plaintiffs' taxable income, that the expenditures made by the plaintiffs in recovering one-fourth of the oil, which oil plaintiffs contend did not belong to them and which expenditures have been allowed by the defendant as deductions in computing petitioners' income taxes for 1933, were erroneously allowed as such deductions. In the determination of plaintiffs' income tax for 1933 the Commissioner of Internal Revenue allowed as deductions the sum of $17,384.85 as expenses spent by plaintiffs in connection with the operation of the leases from which the said sum of $9,614.52 was derived, and that therefore the sum of $4,346.21 (one-fourth of the total expenditures of $17,384.85) represents the plaintiffs' expenditures in connection with the one-fourth of the oil alleged to belong to the plaintiffs' assignors. The defendant therefore alleges that said deduction, amounting to $4,346.21 allowed to the plaintiffs, should be disallowed in determining any refund found by the Court.

Wherefore, defendant having fully answered the first amended petition of plaintiffs herein, prays that plaintiffs take nothing by reason of their suit against him and that he be permitted to go hence without day and recover for costs.

(S.) CLYDE O. EASTUS,
United States Attorney,
(S.) FRANK B. POTTER,
Assistant United States Attorney,
(S.) J. L. BACKSTROM,
Special Attorney,
Treasury Department.

21 In United States District Court

Plaintiffs' motion for judgment

Filed June 11, 1936

To the Honorable Judge of said Court:

Now come the plaintiffs in the above styled and numbered cause and, after the evidence has been heard by the Court, move the Court to render judgment in favor of the plaintiffs for the amount sued for, with interest and costs as provided by law, for under the undisputed facts and the law the plaintiffs are entitled to recover the tax and the interest sued for, together with their costs.

(Signed) HARRY C. WEEKS,
Attorney for Plaintiffs.

WEEKS AND MORROW,
Wichita Falls, Texas,
Of Counsel.

In United States District Court

Judgment

Filed June 19, 1936

This cause came on regularly to be heard on June 11, 1936. The parties appeared, in person and by their attorneys, and announced ready for trial. A jury was waived in writing and all matters of fact, as well as of law, were submitted to the Court. The Court thereupon heard the pleadings and the evidence.

At the conclusion of the evidence, each party moved the Court for judgment in favor of such party. The Court then heard the argument of counsel.

22 Upon consideration of these motions, as well as the pleadings, the evidence and the argument of counsel, the Court determined that the issue presented as to the amount of taxable profit derived by plaintiffs from the sale of their interest in the minerals in and under the west one-half of the Ozier Ranch should be determined in their favor. The Court further determined that they should not prevail as to the other issues presented by them and that their motion for judgment should be granted in part and denied in part and that the defendant's motion for judgment should be granted in part and denied in part. It was accordingly so ordered.

To this, both parties in open Court duly excepted and had their exceptions noted of record.

It is, Therefore, Ordered, Adjudged, and Decreed by the Court that the plaintiffs, J. J. Perkins and wife, Mrs. Lois B. Perkins, do have and recover of and from the defendant, W. A. Thomas, the Collector of Internal Revenue for the Second Collection District of Texas, the sum of one thousand twenty six and 56/100 ($1,026.56) Dollars, together with interest thereon from October 25, 1935, until paid at the rate of six (6%) percentum per annum, and all costs of suit, applicable to issue decided for plaintiffs.

It appearing to the Court that the aforesaid sum was collected by the defendant from the plaintiffs in his aforesaid official capacity as income taxes for the year 1933, and that there was probable cause for action in collecting the sum;

It is Further Ordered by the Court that no execution issue to enforce this judgment, but this judgment shall be, and considered, a certificate of probable cause in favor of said Collector, and this judgement shall be paid by the United States of America in due course as provided by law.

23 To this judgment, both parties excepted in open Court and had their exceptions noted of record.

(Signed) WM. H. ATWELL,
United States District Judge.

In United States District Court

Opinion of the court delivered June 11, 1936

Filed June 17, 1936

J. J. Perkins and wife sue to recover certain income taxes for the year 1933. The first recovery is sought on payments made on what is known as the Ozier ranch deal. There were approximately fifty-four hundred acres of land purchased by the plaintiff, for $10,000.00. He claims that it was bought because of its mineral value, and that the surface was practically valueless. By 1933 he had transferred all of his mineral interests so that from that source he had realized approximately $45.00 per acre. In 1936 he sold the surface for $3.75 per acre. The testimony supports his contention that the venture was attractive because of potential mineral value. Gas and oil were being discovered and were being produced in close proximity. The surface of the land was so rough that it had little value for even ranch purposes. When a transaction in respect to which a loss is claimed, is closed and completed by some identifiable event, then such loss is deductible. Generally this occurs when the property is sold or otherwise disposed of. Coolinga Mohawk Oil Co. v. Commissioner, 64 F. (2) 262. But when a property is of mineral nature and purchased because of that attraction, the bookkeeping need not await the final disposition of the fee provided the testimony is sufficient to show the completion of the mineral transaction. In this case the profits from the mineral part
24 of the land, which motivated the deal, were clearly ascertainable in the year 1933, and the taxpayer was not bounden to wait until the year 1936, when he sold the surface right in order to have a recoupment for his capital investment.

The testimony further shows that a figure of three-quarters for the mineral and one quarter for the surface, is quite generous on the part of the plaintiff.

The second transaction centers around the purchase of oil and gas leases in Gregg County in 1929. $105,000.00 in cash were paid, a note for $50,000.00 was given, which has since been settled, and $395,000.00 more were to be paid out of the oil produced and saved. The contract of sale had these provisions:

"Now, therefore, in consideration of the sum of ten dollars ($10.00) cash in hand paid by Faith Oil Corporation, a Texas corporation, and of the further sum of Three Hundred Ninety-five Thousand Dollars ($395,000.00) to be paid out of the oil produced and saved from the hereinafter described lands, and to be one fourth of all the oil produced and saved from the premises hereinafter described until the full sum of three hundred ninety five thousand dollars ($395,000.00) is paid, we, the said Mamie S. Hammonds, joined by her husband, O. O. Hammonds, and Fred P. Branson,

all of Oklahoma City, Oklahoma County, Oklahoma, the present owners of said leases hereinafter described and all rights thereunder and incident thereto, do hereby bargain, sell, transfer, assign, and convey all our right, title, and interest in and to said leases and rights thereunder, hereinafter described, except the five acres specially excepted therefrom, to Faith Oil Corporation, its successors and assigns, to-wit:"

There follows a detailed description of the oil and gas leases
25 and lands covered thereby which are not material to the question involved. The instrument further provided as follows:

"As hereinbefore stated, three hundred ninety five thousand dollars ($395,000.00) is to be paid to Mamie S. Hammonds and Fred P. Branson, each to receive one half thereof out of the oil produced and saved from said leased premises, which payments shall be made by the pipe line company or other purchaser of said oil, and shall be one fourth (¼) of all the oil produced and saved from the above described land until the full sum of three hundred ninety five thousand dollars ($395,000.00) is fully paid, which oil payments shall be made direct to the said Mamie S. Hammonds and Fred P. Branson, or their heirs and assigns, one half to each, by the purchaser or purchasers of said oil, when and as the same is run. It is understood and agreed that the said three hundred ninety-five thousand dollars ($395,000.00) is payable out of oil only, if, as and when produced from said lands above described, and said oil payment does not constitute and shall not be a personal obligation of the assignee its successors or assigns, nor impose any implied obligation with respect to drilling or development except in contract of June 30, 1931, the intention being that said three hundred ninety five thousand dollars ($395,000.00) shall be paid only out of and to the extent of the proceeds of one fourth of the oil produced and saved from said premises, if, as and when produced.

"It is further agreed and understood that the oil payment herein specified shall bear none of the expenses of the development of said leases or any other burden."

At the time of the making of the leases to the plaintiffs, there were no producing wells. Now there are twenty-two on the Burnett,
26 eight on the Fuller, and eight on the Fenton. Approximately one-half of the $395,000.00 oil payment had been paid up to March 13, 1936, and the balance will probably be paid within two and a half years, if production continues.

There is another tract in Upshur County, which was to be paid for by $45,000.00 in oil, but because of the Court's view with reference to the case it need not concern us.

The plaintiffs were required to include as a part of their income the amount which they derived from the operation of the oil properties, and which they paid to their assignors under the assignment

above quoted. They sue for such amounts. They were allowed depletion.

A case almost directly in point against the plaintiffs' contention is Homer Oil Company v. Burnett, 64 F. (2) 965, Cr. Ct. Ap. Eight Cr. In that case Palmer v. Bender, 287 U. S. 553, is cited.

Counsel for the plaintiffs claim that Palmer v. Bender does not support the view taken in that case, and also calls attention to Commissioner v. Flemming, 82 F. (2) 325, Fifth Circuit.

Palmer v. Bender uses the phrase "economic interest." Economic interest has always been considered, but we have not looked at it in exactly the form presented in the Flemming case. We have thought of it as an equitable interest—a mortgagee's interest. Some kind of unmeasured but clearly defined equity which may be asserted if and when the buyer proves recreant. The phrase appears in a depletion case.

Commissioner v. Flemming is also a depletion case. Neither Palmer v. Bender nor Commissioner v. Flemming deals with the obligation of the purchaser, except inferentially. In Commissioner v. Flemming this language is used:

"While the contract was phrased as though the lease and all
27 of the oil were sold, and as though the proceeds were to be paid back to the seller, the real essence of the contract was that the lease was sold and all the oil Except that whose proceeds were to come to the selling taxpayer. The conveyances executed when the cash was paid might very appropriately have reserved or excepted sufficient oil from one half of that thereafter run, to pay the agreed sum. It is true that no royalty to continue indefinitely was reserved, and that the reservation was limited, not to so many barrels, nor to such a length of time, but to so much oil as would sell for the agreed sum. But it was in effect an exception or reservation of oil. The thing sold for the cash consideration was the lease and all of the oil except that so reserved. If the wells had been agreed to be operated before conveyance, until the sellers should receive this oil payment, it is evident that the depletion allowance would apply to his income from the oil. The source of the income and the seller's economic interest in the production of the oil was exactly the same under the agreement that was made. He is equally entitled to the depletion allowance. The purchaser could in no justice claim it as a deduction from his income."

In Pugh v. Commissioner, Judge Sibley, again writing, 49 F. (2) 76, held that the transfer in that case was a sale, as it showed itself to be.

"We construe this to be a conveyance, operative from its date, of a half interest in the royalty right for a total consideration of $250,000.00, $50,000.00 being paid in cash and the special arrangement being made for the payment of the remainder. The arrangement did not involve Eastham in personal liability, but appropriated

the proceeds of his royalty oil to the payment of Pugh, the seller, until $200,000.00 should be paid. It is specially referred to, as the half belonging to Eastham. As the oil was produced, that due to this half of the royalty right was Eastham's oil. The
28 risk of market price was his. When the proceeds were paid over to Pugh, they were paid, not because the oil was Pugh's, but because it was pledged to Pugh. The money went to discharge the price due on Eastham's purchase, and to pay for the right which he had bought."

It will be noted that neither Perkins, the purchaser, nor the purchasers in either the Pugh or the Flemming cases, assume any personal liability. They are identical, so far as that part of the trade is concerned. Flemming and Pugh were royalty holders and were granted relief from income on the ground that what they thought sold, was really not sold. Perkins, in the present case, the purchaser, not the royalty owner, claims relief on the ground that even though he did buy it, the soul of the transaction shows that the seller did not sell that quarter of the oil out of which he, the seller, was to be paid, to Perkins.

I do not see what right this Court has to construe a plain contract between citizens, which does not need any construing, and then say that it does not mean exactly what it says. The contract between Perkins and those who sold to him, provides that "The present owners * * *, do hereby bargain, sell, transfer, assign, and convey all of our rights, title, and interest in and to said leases and rights thereunder * * *." Again, "It is understood and agreed that said $395,000.00 is payable out of oil only, if as and when produced from said lands above described, and said oil payment does not constitute and shall not be a personal obligation of the assignee, its successors or assigns, nor impose any implied obligations with respect to drilling * * *, the intention being that said $395,000.00 shall be paid only out of and to the extent of the proceeds of one-fourth of the oil produced and saved from said premises, if and when produced."

Certainly the seller has an economic interest in the one-
29 fourth. The taking out of the one-fourth depleted the reservoir from which was to come the oil that would pay him. It also depleted the reservoir that Perkins had bought; therefore, each was allowed depletion. But when payments out of that reservoir were made on what Perkins had promised to pay for it, it was income, so far as he was concerned. If it is not his property, then he could never pay the debt with it. He would merely be handing over to the seller what was already the seller's. It seems to me that Perkins bought that oil. He paid a large part of the purchase price in cash. The remainder he was to pay out of the oil as it was produced. If there was not enough oil to pay the entire unpaid portion, then he owed nothing more. It was oil that was bought and sold. The amount of the oil so bought and sold was unknown.

Quite true the seller has an economic interest in it, in the sense that he will be protected and will be able to follow that oil wherever he can find it. He may reduce it, or, its proceeds to possession. It is subject to his process. Because of his equity in it, his economic interest must be satisfied. In order to hold otherwise, we must disregard all of our basic learning. We find ourselves at a loss to find any harmony in the thought that a seller sells and yet he does not sell. When citizens contract for a purchase and sale and then find the Court construing their contract of purchase and sale to mean something else, when upon its face it is perfectly clear, it is confusing.

If we view the title to the oil as vesting in the buyer, subject to the rights of the seller, we escape such confusion. A recent case by the Circuit Court of Appeals for this Circuit is helpful. Standley v. Graham Production Company, decided May 7, 1936. Judge Foster stated that the assignment did not create an estate in the land, but only a lien on the oil after it had been separated from the soil.

Perhaps a Court should never be concerned with economic result of a holding, but a Court cannot close its eyes to the far-reaching effect of a decision which would make a purchaser unconcerned, so far as his income tax return is viewed, by the amount that he is able to pay the one from whom he buys. Literally hundreds of millions of dollars that have been paid for oil leases and oil lands in Texas, to the sellers thereof, would be swept aside as income, and, for which accounting has been made to the government, if we intimate that because a seller has an economic interest in what he conveys to his buyer, on credit, that therefore, the buyer should be allowed to set aside the explicit words of purchase and say that he really only bought that portion of the property which was evidenced by such returns as he did not have to pay on the purchase price. Such a thought is revolutionary in the field of contracts and a serious attack upon the legal definition of income.

A judgment may be prepared for the plaintiffs, giving them a recovery on the Ozier ranch mineral transaction, and against the plaintiffs on their contention as to oil income.

(Signed) WM. H. ATWELL,
United States District Judge.

At Dallas, Texas, June 11, 1936.

In United States District Court

Motion for extension of term of court

Filed June 30, 1936

Come now the plaintiffs, J. J. Perkins and wife, Mrs. Lois Perkins, by and through their attorney of record, and move the Court that

the present term of this Court be continued as to this cause for a period of seventy-five (75) days so that the plaintiffs may pre-
31 pare and have settled such statement of evidence, bill of exceptions and other matters as the plaintiffs may deem necessary and proper.

(Signed) WEEKS & MORROW,
HARRY C. WEEKS,
Attorneys for Plaintiffs.

Staley Building, Wichita Falls, Texas.

In United States District Court

Order granting extension of term of court

Filed June 30, 1936

On this the 30 day of June, A. D. 1936, came on to be heard the motion of plaintiffs that the present term of the Court be continued, as to this cause, for a period of seventy-five (75) days; and the same having been considered by the Court, it is hereby ordered and decreed that the present term of this Court be, and the same is hereby, continued and extended, as to this cause, for seventy-five days from and after this date, so that the plaintiffs may prepare and have settled such statement of evidence, bill of exceptions, and other matters as the plaintiffs may deem necessary and proper.

(Signed) WM. H. ATWELL,
United States District Judge.

In United States District Court

Bill of exceptions

Filed July 7, 1936

Be It Remembered that on the trial of this cause on June
32 11, 1936, the Honorable William Hawley Atwell, United States District Judge, presided, and both parties appeared by counsel. A jury was waived in writing and the following proceedings were had:

I

Both parties presented their pleadings to the Court.

II

By agreement with defendant, the plaintiffs introduced in evidence the evidence heard at the previous trial of this cause, which evidence is as follows:

J. J. PERKINS, being first duly sworn, examined in chief by Mr. Weeks, testified as follows:

My name is J. J. Perkins. I am one of the plaintiffs in this case, my wife is the other plaintiff. I live in Wichita Falls. I have been married sixteen or eighteen years. I am in the oil producing business, more than any other business, and have been about twenty years. I have been active in that business during that time. The major portion of my time has been devoted to producing oil and purchasing oil properties, oil royalties. I give my oil business my personal attention, and have been doing so continuously since I started in that business. I am familiar with the trade practices and customs in the oil business in Texas.

In 1931 I became interested in some oil properties in East Texas, with W. J. Green and the Faith Oil Corporation. Some properties were bought from Branson and Hammonds, and the purchase was made in the name of the Faith Oil Company and was one-
33 fourth for the Faith Oil Company, one-half of the other three-fourths for me, and the other half for W. J. Green, subject to such advances as he might owe. The Faith Oil Corporation, was incorporated, and Mr. Green and I were stockholders in it; Mr. Green was president and I was not an officer or director at that time, but one of the largest stockholders.

There was quite a substantial acreage involved in the purchase from Branson and Hammonds, but only about two hundred and fifty acres in the main portion of the field. The property was not producing at the time we acquired it from Branson and Hammonds. This is a copy of the instrument by which we acquired the property from them.

Mr. WEEKS. We offer the instrument in evidence.

Plaintiff's Exhibit No. 1

THE STATE OF TEXAS,
County of Gregg.

Whereas, Mamie S. Hammonds and Fred P. Branson are the owners of certain oil and gas leases in Gregg and Upshur Counties, Texas, on the lands hereinafter described, and are owners of all rights thereunder or incident thereto.

Now, Therefore, in consideration of the sum of Ten Dollars ($10.00), cash in hand, paid by Faith Oil Corporation, a Texas Corporation, and of the further sum of Three Hundred Ninety Five Thousand Dollars ($395,000.00) to be paid out of the oil produced and saved from the hereinafter described lands, and to be one-fourth of all the oil produced and saved from the premises hereinafter described, until the full sum of Three Hundred and Ninety Five
34 Thousand Dollars ($395,000.00) is paid, we, the said Mamie S. Hammonds, joined by her husband, O. O. Hammonds, and Fred P. Brandon, all of Oklahoma City, Oklahoma County, Okla-

homa, the present owners of said leases hereinafter described and all rights thereunder and incident thereto, do hereby bargain, sell, transfer, assign, and convey all our rights, title, and interest in and to said leases and rights thereunder, hereinafter described, except the five acres specially excepted therefrom, to Faith Oil Corporation, its successors and assigns, to-wit:

"Detailed descriptions of oil and gas leases omitted in printing because the same are immaterial to any issue. The instrument assigned oil and gas leases made by the following original lessor: D. W. McQueen and wife; J. J. Fuller and wife; E. E. Stone and Wife; J. C. Barrett, B. B. Fenton; Mrs. Lucille Thrasher et al.; J. M. Hamby and wife", as per stipulation of counsel copied at page one hereof.

* * * * * * *

As hereinbfore stated, Three Hundred Ninety Five Thousand Dollars ($395,000.00) is to be paid to Mamie S. Hammonds and Fred P. Branson, each to receive one-half thereof, out of the oil produced and saved from said leased premises, which payments shall be made by the pipe line company or other purchaser of said oil, and shall be one-fourth (¼) of all the oil produced and saved from the above described land, until the full sum of Three Hundred Ninety Five Thousand Dollars ($395,000.00) is fully paid, which oil payments shall be made direct to the same Mamie S. Hammonds and Fred P. Branson, or their heirs and assigns, one-half to each, by the purchaser or purchasers of said oil, when and as the same is run. It is understood and agreed that the said Three Hundred Ninety-
35 five Thousand Dollars ($395,000.00) is payable out of oil only, if, as and when produced from said lands above described, and said oil payment does not constitute and shall not be a personal obligation of the assignee, its successors or assigns, nor impose any implied obligation with respect to drilling or development, except in contract of June 30, 1931, the intention being that said Three Hundred Ninety-five Thousand Dollars ($395,000.00) shall be paid only out of and to the extent of the proceeds of one fourth of the oil produced and saved from said premises, if, as and when produced.

It is further agreed and understood that the oil payment herein specified shall bear none of the expenses of the development of said leases or any other burden.

And for the same consideration, the said Mamie S. Hammonds, joined by her husband, O. O. Hammonds and Fred P. Branson, and their heirs and legal representatives, covenant with the said Faith Oil Corporation, its successors and assigns, that they are the lawful owners of said leases and interest thereunder, and of the personal property thereon or used in connection therewith; that they have good right and authority to sell and convey the same, and that said rights, interest, and property are free and clear from all liens and encumbrances, and that all rentals and royalties due and payable thereunder have been duly paid, and that they do hereby warrant

and agree to defend the title to said leasehold estate in the lands above described against the lawful claims and demands of all persons, whomsoever.

In Witness Whereof, the said Mamie S. Hammonds, O. O. Hammonds and Fred P. Branson, have signed this instrument, this the 24 day of July, A. D. 1931.

(Signed) MAMIE S. HAMMONDS.
O. O. HAMMONDS.
FRED P. BRANSON.

36 "Acknowledgments and recording data omitted because immaterial," as per stipulation of counsel copied at page one hereof.

* * * * * * *

Mr. WEEKS: For the purpose of showing the nature of the interest of Branson and Hammonds, we offer in evidence Plaintiff's Exhibits 2, 3, and 4, as follows:

Plaintiff's Exhibit 2

Oil and Gas Lease

Agreement, made and entered into the 29th day of July 1930, by and between B. B. Fenton and Wife, Myra Fenton, of Gregg County, Texas, hereinafter called lessor (Whether one or more), and J. A. Reynolds, hereinafter called lessee:

Witnesseth: That the said lessor, for and in consideration of One Dollars cash in hand paid, receipt of which is hereby acknowledged, and of the covenants and agreements hereinafter contained on the part of lessee to be paid, kept and performed, has granted, demised, leased, and let and by these presents does grant, demise, lease and let unto the said lessee, for the sole and only purpose of mining and operating for oil and gas, and laying pipe lines, and building tanks, power stations, and structures thereon to produce, save, and take care of said products, all that certain tract of land situated in the County of Gregg, State of Texas, described as follows, to-wit: All that certain tract, lot or parcel of land situated in Gregg County,

37 Texas, about 9½ miles from Longview, a part of M. Irwin H. R. Survey No. 19, beginning at R. P. Doby's N. W. Corner on the Irwin Line a stake for Corner from which a Pine brs. N. 78½ E. 2.6 vrs. Thence N. 498 vrs. to said Irwin's N. W. Corner a stake from which a Red Oak Brs. S. 20 E. 13.6 vrs. Thence E. 566.8 vrs. a stake for corner from which a Post Oak brs. S. 57 W. 92 vrs. A Hickory brs. N. 27 E. 12 vrs. Thence 498 vrs. to N. W. Corner of Pleas Doby's 50 acre tract, and N. W. Corner J. H. Satterwhites 14 acre tract. Thence W. 566.8 vrs., to place of beginning, containing 50 acres, declination of the Needle 8½ Degrees. Recorded in Book 54, Page 47. Being all the land I own in Gregg County, and containing 50 acres, more or less.

It is understood that this lease shall remain in force for a term of 5 years from date, and as long thereafter as oil or gas, or either of them, is produced from said land by the lessee.

In consideration of the premises the said lessee covenants and agrees:

1st. To deliver to the credit of lessor, free of cost, in the pipe line to which lessee may connect his wells, the equal one-eighth part of all oil produced and saved from the leased premises.

2nd. To pay to lessor, as royalty for gas from each well where gas only is found, while the same is being sold or used off of the premises, one-eighth of the market price at the wells of the amount so sold or used, the lessor to have gas free of charge from any gas well on the leased premises for all stoves and inside lights in the principal dwelling house on said land by making lessor's own connections with the well at lessor's own risk and expense.

3rd. To pay to lessor as royalty for gas produced from any
38 oil well and used by lessee for the manufacture of gasoline, one-eighth of the market value of such gas. If such gas is sold by lessee, then lessee agrees to pay lessor, as royalty, one-eighth of the market price at the wells of the amount sold.

If no well be commenced on said land on or before the 1st day of Dec. 1930, this lease shall terminate as to both parties, unless the lessee on or before that date shall pay or tender to the lessor, or to the lessor's credit in the 1st National Bank at Longview, Texas, or its successors, which shall continue as the depository regardless of changes in the ownership of said land, the sum of $50 Dollars, which shall operate as a rental and cover the privilege of deferring the commencement of a well for 12 months from said date. In like manner and upon like payments or tenders the commencement of a well may be further deferred for like periods of the same number of months successively. And it is understood and agreed that the consideration first recited herein, the down payment, covers not only the privilege granted to the date when said rental is payable as aforesaid, but also the lessee's option of extending that period as aforesaid and any and all other rights conferred.

Should the first well drilled on the above described land be a dry hole, then, and in that event, if a second well is not commenced on said land within twelve months from the expiration of the last rental period, which rental has been paid, this lease shall terminate as to both parties, unless the lessee on or before the expiration of said twelve months shall resume the payment of rentals in the same amount and in the same manner as hereinbefore provided. And it is agreed that upon the resumption of the payment of rentals, as above provided, that the last preceding paragraph hereof, governing the payment of rentals and the effect thereof, shall continue in force just as though there had been no interruption in the rental payments.

If, at the expiration of 5 years from the date of this lease, oil or gas is not being produced on the leased premises, but lessee is then engaged in drilling for oil or gas, then this lease shall continue in force so long as drilling operations are being continuously prosecuted on the leased premises; and drilling operations shall be considered to be continuously prosecuted if not more than sixty (60) days shall elapse between the completion or abandonment of one well and the beginning of operations for the drilling of a subsequent well. If oil or gas shall be discovered and produced in paying quantities from any such well or wells drilled at or after the lapse of 5 years, this lease shall continue in force so long as oil or gas shall be produced from the leased premises.

It is specially agreed that in the event that oil or gas is produced from said premises and said production shall for any reason cease or terminate, lessee shall have the right at any time within ninety (90) days from the cessation of such production to resume drilling operations in the effort to make said leased premises again produce oil or gas, in which event this lease shall remain in force so long as such operations are continuously prosecuted, as defined in the preceding paragraph, and if they result in production of oil or gas, so long thereafter as oil or gas is produced in paying quantities from the premises.

If said lessor owns a less interest in the above described land than the entire and undivided fee simple estate therein, then the royalties and rentals herein provided for shall be paid the said lessor only in proportion which lessor's interest bears to the whole and undivided fee.

Lessee shall have the right to use, free of cost, gas, oil, and water produced on said land for all operations thereon, except from water wells of lessor. When requested by lessor, lessee shall bury its pipe line below plow depth. No well shall be drilled nearer than 200 feet to the house or barn now on said premises without the written content of the lessor. Lessee shall pay for damages caused by all operations to growing crops on said land. Lessee shall have the right at any time to remove all machinery and fixtures placed on said premises, including the right to draw and remove casing.

If the estate of either party hereto is assigned, and the privilege of assigning in whole or in part is expressly allowed, the convenants hereof shall extend to their heirs, executors, administrators, successors or assigns, but no change in the ownership of the land or assignment of rentals or royalties shall be binding on the lessee until after the lessee has been furnished with a written transfer or assignment or a true copy thereof, and it is hereby agreed in the event this lease shall be assigned as to a part or parts of the above described lands and the assignee or assignees of such part or parts shall fail or make default in the payment of the proportionate part

of the rents due from him or them, such default shall not operate to defeat or affect this lease in so far as it covers a part or parts of said lands upon which the said lessee or any assignee thereof shall make due payment of said rental.

Lessee shall have the exclusive right to build, operate, and maintain pits, reservoirs, pickup stations, and plants for the purpose of picking up and conserving the waste oil that flows down the creeks, ravines, and across the land embraced in this lease whether said oil is produced from lands covered by this lease or other lands and lessor shall be entitled to receive the royalty hereinbefore reserved on all such oil so saved.

In case of cancellation or termination of this lease for any
41 cause, lessee shall have the right to retain under the terms hereof twenty (20) acres of land around each oil or gas well producing, being worked on, or drilling hereunder (as long as such operations are continued in good faith) such tract to be designated by lessee in as near as a square form as practicable.

In the event lessor considers that lessee has not complied with all its obligations hereunder, both express and implied, before production has been secured or after production has been secured, lessor shall notify lessee in writing, setting out specifically in what respects lessee has breached this contract. Lessee shall then have sixty (60) days after receipt of said notice within which to meet or commence to meet all or any part of the breaches alleged by lessor. The service of said notice shall be precedent to the bringing of any action by lessor on said lease for any cause, and no such action shall be brought until the lapse of sixty (60) days after service of such notice on lessee. Neither the service of said notice nor the doing of any acts by lessee aimed to meet all or any of the alleged breaches shall be deemed an admission or presumption that lessee has failed to perform all its obligation hereunder.

Title to the minerals vested in grantee under this grant shall not end or revert to grantor until there is a complete, absolute, and intentional abandonment by grantee of each and all of the purposes expressed or implied, of this grant and every part and parcel of the premises described in this grant.

Lessor hereby warrants and agrees to defend the title to the lands herein described, and agrees that the lessee shall have the right at any time to redeem for lessor by payment, any mort-
42 gage, taxes, or other liens on the above described lands, in the event of default of payment by lessor, and be subrogated to the rights of the holder thereof, and lessor hereby agrees that any such payment made by the lessee for the lessor shall be deducted from any amounts of money which may become due the lessor under the terms of this lease.

In Testimony Whereof, we sign, this the 29th day of July 193—.

(Signed) B. B. FENTON,
MYRA FENTON.

"Acknowledgments and recording data omitted because immaterial", as per stipulation of counsel copied at page one hereof.

* * * * * * *

Plaintiff's Exhibit 3

"This Exhibit was an oil and gas lease from J. C. Barrett to J. A. Reynolds, dated August 26, 1929, and, except as to parties and descriptions, is identical with Exhibit 2 and is therefore omitted", as per stipulation of counsel copied at page one hereof.

* * * * * * *

Plaintiff's Exhibit 4

Oil and Gas Lease.

"This Exhibit was an oil and gas lease from J. J. Fuller and wife to Mamie S. Hammonds, dated September 22, 1930, and, except for parties and descriptions, is identical with Plaintiff's Exhibit 2, and is therefore omitted in printing" as per stipulation of counsel copied at page one hereof.

* * * * * * *

43 The WITNESS. This assignment, Plaintiff's Exhibit 1, dated July 24, 1931, was originally in the name of the Faith Oil Corporation, and Mr. Green and I were interested with that corporation to the extent of three-fourths. This instrument recited a consideration of $10.00 in addition to this oil payment, but that was not the consideration; the consideration was $105,000.00 in cash and some notes for $50,000.00, which were later paid, making a total of $155,000.00. The Green-Perkins interest, which stood in the name of the Faith Oil Corporation, were later assigned to me. This is a copy of the assignment; there were two such assignments, both of these are copies of the original.

Mr. WEEKS. We offer in evidence the assignments placing the record title to Perkins and Green interest, which had been in the name of the Faith Oil Corporation, in the name of Mr. Perkins. We offer the instruments in evidence as Plaintiff's Exhibit 5–a and 5–b, as follows:

Plaintiff's Exhibit 5–a

STATE OF TEXAS, *County of Gregg:*

Whereas Faith Oil Corporation holds in its own name the record title to the hereinafter described oil and gas leases situated in Gregg and Upshur Counties, Texas, as hereinafter set out, while the real ownership of said leases is owned three-fourths (¾) by J. J. Perkins, and one-fourth (¼) by said Faith Oil Corporation and all rights thereunder or incident thereto in connection with said oil and gas lease.

Now, Therefore, in consideration of the sum of Ten Dollars
44 ($10.00) cash in hand paid by J. J. Perkins to Faith Oil Corporation, a Texas Corporation, the receipt of which is hereby acknowledged and for the purpose of vesting the record title of said leases according to their actual ownership the said Faith Oil Corporation, acting by and through its duly authorized President, W. J. Green, does hereby bargain, sell, transfer, assign and convey unto the said J. J. Perkins an undivided three-fourths (¾) interest in and to said oil and gas leases and all rights thereunder, as hereinafter set out (the said Faith Oil Corporation retaining an undivided one-fourth (¼) interest in and to said oil and gas leases); there having been executed an assignment of certain oil and gas leases dated July 24, 1931, and filed in the Gregg County Deed Records on July 28, 1931, at 1:10 P. M., and recorded in Volume —, Page —, Gregg County Deed Records, File No. 21719, from Mamie S. Hammonds and husband, O. O. Hammonds, and Fred P. Branson to Faith Oil Corporation and reference is here made to said assignment for a better description of the lands covered by said oil and gas leases in and to which an undivided three-fourths (¾) interest is hereby conveyed by said Faith Oil Corporation to J. J. Perkins, which leases are described as follows, to-wit:

First: An oil and gas lease from D. W. McQueen and wife covering a part of the H. F. Rogers, James Price, and Dan Meredith H. R. Surveys containing 192 acres of land, more or less, and being described in a deed of Trust to Federal Land Bank, as shown in Volume 11, page 131, Deeds of Trust Records of Gregg County, Texas, with the exception of 60 acres leased out of said above described land.

Second: An oil and gas lease executed by E. E. Stone and wife, Blanche Stone, covering 51.7 acres more or less out of H. H. Kirk Headright Survey about 8 miles north of Longview, Texas.

45 Third: An oil and gas lease executed by J. C. Barrett covering all of the B. W. Witcher Headright Survey situated about 10 miles north of Longview, Texas, except the north 100 acres of said Witcher Survey, and except 80 acres assigned by Mamie S. Hammonds, et vir, to Shell Petroleum Corporation, dated January 10, 1931.

Fourth: An oil and gas lease executed by Mrs. Lucile Thrasher et al., and recorded in Book 4, Page 549-551, Gregg County Deed Records covering 55½ acres of land out of H. H. Kirk Headright Survey.

Fifth: An oil and gas lease executed by J. M. Hamby and wife and recorded in Book 59, Page 622, Gregg County Deed Records and covering 320 acres more or less out of the John Lout Headright Survey in Gregg County, Texas, and also 50 acres of land more or less out of the Chas. P. Hereford Headright Survey and recorded in Volume X, page 246, Gregg County Deed Records.

In said assignment made by Mamie S. Hammonds et al. to Faith Oil Corporation there was retained in said conveyance an oil payment to the extent of $395,000.00 to be paid out of one-fourth of all the oil produced and saved from the lands described in said assignment and this conveyance is made by Faith Oil Corporation to J. J. Perkins subject to said oil payment, as is fully set out in said assignment above mentioned.

(The object and intention of this conveyance is not to increase or to decrease in any way the burdens upon said leases, or any one of them, but to vest in said J. J. Perkins an undivided three-fourths (¾) interest in said leases and retain in the Grantor herein
46 an undivided one-fourth (¼) interest in said leases subject to said oil payment); and for the same consideration the said Faith Oil Corporation, its successors and assigns covenant and agree with the said J. J. Perkins, his heirs and assigns, that it is the lawful owner of said leases and interest thereunder and the personal property thereon, or used in connection therewith and that it has good right and authority to sell and convey the same and that said rights, interests, and property are free and clear of any liens and incumbrances except as shown by the Gregg County Deed Records and that all rentals and royalties due and payable thereunder have been duly paid and it does hereby warrant and agree to protect the title to said leasehold estate and the lands above described against the lawful claims and demands of any person whomsoever to the extent of the interest hereby conveyed.

In Testimony Whereof Witness its name and corporate seal on this the 4th day of June, A. D. 1932.

FAITH OIL CORPORATION,
By W. J. GREEN, *President.*

Attest:
[SEAL]

JOHN C. COFFEY,
Secretary.

"Acknowledgments and recording data omitted because immaterial", as per stipulation of counsel copied at page one hereof.

* * * * * * *

Plaintiff's Exhibit 5-b

THE STATE OF TEXAS,
County of Gregg.

Whereas, Mamie S. Hammonds and husband, O. O. Hammonds, and Fred P. Branson of Oklahoma City, Oklahoma,
47 did on or about July 24, 1931, transfer, assign, and convey unto Faith Oil Corporation certain oil and gas leases situated in Gregg County, Texas, reference being made to said recorded instruments for the description of the properties covered thereby and the terms of said conveyance, and did in said assignment convey

what is known as the J. J. Fuller lease, which is recorded in Book 5, Page 381, which is described as follows:

All that certain lot, tract, or parcel of land being situated in Gregg County, Texas, about 8½ miles N. W. from the town of Longview and being a part of the M. A. Alexander H. R. Survey; Beginning at the N. E. corner of the old Wm. Fuller tract, a stake from which a black jack brs. S. 8½ E. 7 vrs.; thence S. 359 vrs. to a stake from which a double red oak brs. S. 50 E. 7 vrs.; thence in a westernly direction with an old cross fence 372 vrs. to a stake from which a small red oak brs. N. 26 E. 2 vrs. a Post Oak brs. E. 2 vrs.; thence S. 75 W. 20 vrs., a stake from which a Black Jack brs. N. 76 W. 7 vrs.; thence S 23 vrs. W. 123 vrs. a stake from which a Red Oak brs. S. 84 W. 9 vrs.; thence S. 56 W. 343 vrs. a stake from which a red Oak brs. N. 55 W. 8 vrs.; thence N. 81 W. 116 vrs. a stake from which a Post Oak brs. N. 30 W. 18 vrs.; thence S. 22 W. 125 vrs. to a stake; thence N. 70 W. 30 vrs. a stake from which a walnut brs. N. 4 W. 2 vrs.; thence S. 20 W. 50 vrs. a stake from which a black jack brs. S. 78 W. 8 vrs.; thence S. 45 W. 66 vrs to a stake in the E. B. Line of Maury Irwin Survey a pipe brs. S. 58 E. 3 vrs.; thence N. with Irwin's E. B. line 620 vrs. to the N. W. corner of the Wm. Fuller home tract a stake near the root of a fallen tree; thence E. 750 vrs. to place of beginning containing in all 56 4/10 acres of land more or less. But from this lease is excepted approximately 5 acres in the S. W. corner thereof.

48 Said lease is duly recorded in Book 4, Pages 211 to 212, Oil & Gas Lease Records of Gregg County, Texas.

And, also, an assignment of oil and gas lease executed by B. B. Fenton which lease is recorded in Vol. 59, Page 610, Gregg County Deed Records, which land is described as follows, to-wit:

All that certain tract, lot or parcel of land situated in Gregg County, Texas, about 9½ miles from Longview a part of M. Irwin H. R. Survey No. 19; Beginning at R. P. Doby's N. W. corner on the Irwin Line, a stake for corner from which a pine brs. N. 78½ E. 2.6 vrs.; thence N. 498 vrs. to said Irwin N. W. corner a stake from which a read oak brs. S. 20 E. 13.6 vrs.; thence E. 566.8 vrs. a stake for corner from which a post oak brs. S. 57 W. 92 vrs. a hickory brs. N. 27 E. 12 vrs.; thence 498 vrs. a N. W. corner of Pleas Doby's 50 acre tract and N. W. corner of J. H. Satterwhite's 14 acre tract; thence W. 566.8 yrs. to place of beginning containing 50 acres; declination of the Needle 8½ deg. Recorded in Book 54, Page 47, which assignment covers other lands as well but which are not under consideration at this time, and

Whereas, J. J. Perkins is the owner of an undivided three-fourths (¾) interest in and to said two above described leases, though as a matter of convenience the record title has been in the Faith Oil Corporation and it is the desire of Faith Oil Corporation and J. J. Perkins that a instrument be executed placing the record title to

J. J. Perkins' undivided three-fourths (¾) interest in and to said leases in him so that the records may disclose the true ownership.

Now, therefore, for and in consideration of Ten Dollars
49 and other good and valuable considerations, the receipt of which is hereby acknowledged, and for the purpose of setting out the actual ownership in said property, the said Faith Oil Corporation does hereby bargain, sell, transfer, assign, and convey unto the said J. J. Perkins of Wichita County, Texas, an undivided three-fourths (¾) interest in and to said above described two leases known as the J. J. Fuller lease and the B. B. Fenton lease and hereinbefore described by metes and bounds, together with all personal property used or obtained in connection therewith to J. J. Perkins, his heirs and assigns, and for the same consideration the said Faith Oil Corporation for itself, its successors and assigns does covenant with the said J. J. Perkins, his heirs and assigns that it is the lawful owner of said leases and all rights and interest thereunder and of the personal property thereon or used in connection therewith; that it has good right and authority to convey the same and that it will warrant and forever defend the same against the lawful claim and demands of all persons whomsoever.

This conveyance, however, is made subject to the contingent oil payment as contained in the assignment from Mamie S. Hammonds et al., above referred to.

The object and intention of this instrument being to vest title to an undivided three-fourths (¾) interest in and to said above two described leases in J. J. Perkins and retain in the Grantor herein an undivided one-fourth (¼) interest in the two above described leases without in any way increasing or decreasing the burdens and obligations of said properties.

In Testimony Whereof witness its name and seal on this 20th day of June A. D. 1932.

FAITH OIL CORPORATION,
[SEAL] By W. J. GREEN, *President.*
Attest: JOHN C. COFFEY,
Secretary.

50 "Acknowledgments and recording data omitted because immaterial", as per stipulation of counsel copied at page one hereof.

* * * * * * *

The WITNESS. We subsequently developed that property for oil. It was in the fall of 1931 that the first well was drilled on the J. J. Fuller lease, and I think it was about the same time that the first well was drilled on the Fenton lease, and the other was the Barrett lease, of about 154 acres, and the first production on that was in the Spring of 1932. We continued to develop it. We had twenty-two wells on the Barrett lease and eight on the Fuller and eight on the Fenton.

I continued through 1933 to own the interest in the property originally acquired; that is, undivided three-eighths interest.

The oil from each lease was run into a battery of tanks on the respective leases, and division orders executed to the pipe line companies, running that oil, the royalty owners received one eighth, Branson and Hammonds, jointly received one-fourth, and the remaining five-eighths going to the Faith Oil Corporation, Green, and myself. I think during the year 1933 perhaps all the checks for our five-eighths were made payable to the Faith Oil Corporation covering my interest and Green's interest, and the Faith's interest. That was done at all times from the time we began producing through 1933, and up to the present time. That oil payment has not been discharged, but it will be some time before it is paid, if ever.

As to the actual receipt of the money, I will state, there was delivered in the pipe line, to the credit of Branson and Hammonds, one-fourth of the oil produced, and I presume the pipe-line companies paid them, because they never paid us. I think I can say
51 I know it was paid, because I discussed it with Judge Branson and Mrs. Hammonds many times, and they would speak of the payments they had received on this lease. I know that we never received a dollar of those payments. I know that is true in respect to the Faith Oil Corporation and W. J. Green. When I spoke of the division orders that were executed, that is the ordinary and customary way of handling that matter in the oil business. These instruments which you hand me are typical of the division orders which were executed in respect to those properties.

Mr. WEEKS: We offer in evidence those four samples of division orders, being typical of the ones that were made.

(Said instruments marked "Plaintiff's Exhibits 6, 6-a, 6-b, and 6-c", and reading as follows:)

Plaintiff's Exhibit 6

Magnolia Petroleum Company

Transfer Order

JUNE 20, 1932.

To MAGNOLIA PETROLEUM COMPANY,
Dallas, Texas:

The undersigned, having transferred, as indicated below, oil production of wells numbered _____ on the Faith Oil Corporation on the J. J. Perkins far, more particularly described as 56.4 acres out of the M. L. Alexander Survey less 5 acres in the southwest part thereof, in Gregg County, State of Texas, you are here-
52 by authorized, beginning at 7 o'clock A. M. on the _____ day of _____ 19__, and until further notice, to give credit for oil received on account of said interest so transferred as follows:

Credit to—	Transferred interest	P. O. address (give box no. or st. address)
J. J. Fuller	3/64 RI	
Frank Buttram	155/3072 RI	
A. W. Gilliland	1/96 RI	
F. W. C. Loyalty Corp	1/64 RI	
Errett R. Newby	5/3072 RI	
Faith Oil Corp'n	20/32 WI	
Mrs. Mamie S. Hammonds	4/32 WI	
Until $197,500 is paid, reverts to Faith Oil Corporation.		
Fred P. Branson	4/32 WI	
Until $197,000 is paid, reverts to Faith Oil Corporation.		

Witness:

The undersigned certify that they are the legal owners of the interest above transferred and warrant the title thereto, and the Magnolia Petroleum Company is hereby authorized, until further notice, to receive oil for purchase from said parties, subject to the following conditions:

1. Quantities are to be computed from regularly compiled
53 tank tables, the oil owner to have the privilege of witnessing gauge tickets, and, in addition to the deductions of the tank tables, corrections shall be made for temperature and impurities according to your local rules in force at the time, and oil shall be steamed when necessary to render it merchantable.

2. Satisfactory abstracts and other evidence of title will be furnished to you at any time on demand. In the event of a failure to so furnish such evidence of title, or in the event of a dispute at any time concerning title, you may hold the oil run or its proceeds, without interest, until indemnity satisfactory to you has been furnished.

3. Runs to Magnolia Pipe Line Company for your account or to any other pipe line company designated by you, shall be valid delivery, and said pipe line company in your place and stead may make the aforesaid deductions and corrections.

4. In the absence of written agreement to the contrary, oil received under this division order shall become your property when delivered to said pipe line company, and shall be paid for to the party or parties according to the divisions of interests shown above at the price posted by Magnolia Petroleum Company for the same kind and quality of oil in the particular field in which it is received

on the day on which it is received by said pipe line company into its custody. For the amount due on account of the oil received during each calendar month, payment shall be made on or before the 12th day of the next succeeding month by mailing Magnolia Petroleum Company's checks therefor to the addresses of said parties respectively as given above, or by deposit of the sum due to the credit of said parties respectively at_____bank at_____. Except that you are authorized to withhold payment due any individual payee until at least five dollars ($5.00) has accu-
54 mulated to the credit of such payee, it being agreed, however, that regardless of amount so accumulated to the credit of such payee, *it being agreed, however, that regardless of amount so accumulated to the credit of such payee* you will, in December of each year, make payment of the full amount so credited to each payee for oil run up to and including the month of November of such year.

5. You are not expected to receive oil in definite quantities or for fixed periods nor to provide storage on the credit balance plan or otherwise except as and when you shall now or hereafter so agree in writing.

6. Sellers severally agree to notify Magnolia Petroleum Company of any change of ownership; it being understood that any vendee or assignee of said wells or the production thereof shall take same subject to the terms hereof.

FAITH OIL CORPORATION.
MAMIE S. HAMMONDS.
FRED P. BRANSON.

Witness:

Plaintiff's Exhibit

Stanolind Crude Oil Purchasing Company

Division Order

AUGUST 1, 1933.

TO STANOLIND CRUDE OIL PURCHASING COMPANY,
Tulsa, Okla.:

The undersigned, and each of them, guarantee and warrant that they are the legal owners in the proportions set out below of all the oil produced from the _____ J. J. Fuller Farm, described as 56.4 acres out of the M. Alexander Survey less 5 acres in the SW. part thereof, more fully described as follows: Beginning at
55 the NE. cor. of the old Wm. Fuller tract; thence So. 359 vrs., a stake; thence in a westerly direction with an old cross fence 372 vrs., a stake; thence So. 75° W. 20 vrs., a stake; thence so. 23° W. 123 vrs.; thence 56° W. 34 vrs., a stake; thence 81° W. 116 vrs., a stake; thence S. 22° W. 125 vrs.; thence N. 70° W. 30 vrs., a stake; thence 20° W. 50 vrs., a stake; thence S. 45° W. 66 vrs., a stake in the EB. L. of Irwin's Survey; thence N. with EB. L. Irwin Sur. 620 vrs. to NW. cor. of Wm. Fuller home tract; thence E. 760 vrs. to

place of beginning in Gregg County, State of Texas, and commencing at 7 a. m. the 1st day of August 1933, and until further written notice either from you or us; you are authorized to receive oil therefrom, purchase it and pay therefor as follows:

Credit to—Div. of Interest—P. O. Address

The First National Bank, Gilmer, Texas. 7/8 W. I.

Subject to the following oil payments:

(1) $197, 500.00 out of 1/7 or 7/8 WI payable to Mrs. Mamie S. Hammonds, 623 E. 18th St., Oklahoma City, Okla.

(2) $197,500.00 out of 1/7 of 7/8 WI payable to Fred P. Branson, c/o Skirvin Hotel, Oklahoma City.

The 1/8 Royalty Interest:

J. J. Fuller, Route 2, Longview, Texas, 3/8.

Frank Buttram, 2908 First National Bank Bldg., Okla. City, Ok., 155/384.

Errett R. Newby, 2909 First National Bank Bldg., Okla. City, Ok., 5/384.

56 Fidelity Royalty Co., 706 Barniff Bldg., Okla. City, Okla., 1/12.

F. W. C. Royalty Corp., Drawer 1866, Houston, Texas, 1/8.

Faith Oil Corp. agrees to notify Stanolind Crude Oil Purchasing Company in writing when the above mentioned oil payments are completed and will hold Stanolind Crude Oil Purchasing Company harmless for any overpayments on said oil payments in the absence of written notice.

The following covenants are also parts of this division order, and shall be binding upon the undersigned, their successors, legal representatives and assigns:

First: The oil run hereunder shall become your property as soon as the same is received into your custody or that of any pipe line company designated by you.

Second: The oil received and purchased pursuant hereto shall be delivered f. o. b. to any pipe line designated by you which gathers and receives said oil, and you agree to pay for such oil to the respective owners according to the division of interest hereinabove indicated, at the price paid by you for similar crude oil in the field where said oil is produced, preva'ling on the date of each respective run; settlements and payments shall be made monthly account oil runs during the preceding month, by check of Stanolind Crude Oil Purchasing Company mailed from Tulsa, Oklahoma, to the respective parties at the addresses above given. Pipe line grades and measurements shall govern and control in all settlements.

Third: You are to receive merchantable oil only under the

57 terms of this division order. The gauging, testing, and correction for temperature of, and deductions from, oil pur-

chased hereunder, shall be in accordance with the Pipe Line Rules and Regulations of the Railroad Commission of Texas.

Fourth: Satisfactory abstracts, or other evidence of title, will be furnished at any time on demand. In the event of failure to furnish such evidence of title, or in the event of any dispute or question at any time concerning the title to said land and/or the oil produced therefrom, you are authorized to withhold the proceeds of all oil received and run, without interest, until such dispute, defect, or question of title is corrected or removed to your satisfaction, or until indemnity satisfactory to you has been furnished; and in the event any action or suit is filed in any Court affecting the title to the land above described or the oil produced therefrom, to which any of the undersigned is a party, written notice of the filing of such suit or action shall be immediately furnished you by the undersigned, stating the Court in which the same is filed and the title of such suit or action.

Fifth: This division order shall become valid and binding on each and every owner above named as soon as signed by him or her regardless of whether or not any of the other above named owners have so signed; and in consideration of the purchase of oil hereunder, consent is hereby given to you and/or any pipe line company which you may cause to connect with the wells and/or tanks on said land, to disconnect and remove such pipe lines, in case of termination by either you or us of purchases under this division order.

Sixth: The undersigned, and each of them, guarantee and warrant, for your benefit and that of any pipe line or other carrier designated by you to run or transport said oil, that all oil tendered hereunder has been produced in accordance with the laws of Texas and the rules and regulations of the Railroad Commission of Texas.

58

FAITH OIL CORPORATION,
By W. J. GREEN, *President.*
FIRST NAT'L BANK, GILMER, TEXAS,
By H. P. MCGAUGHY, *President.*
F. W. C. ROYALTY CORPORATION,
By A. W. CROSBY, *Vice-President.*
FRED P. BRANSON.
MAMIE S. HAMMONDS.
J. J. PERKINS.

Witnesses:
[SEAL]
S. A. MAN, *Secretary.*
Attest:
L. B. MARTIN, *Cashier.*

Attest:
G. U. WATSON, *Secretary.*

Please insert correct address.

Plaintiff's Exhibit 6-a

OP-150

Simms Oil Company

Division Order

MAY 10TH, 1933.

To SIMMS OIL COMPANY:

The undersigned certify and guarantee that they are the
59 legal owners of wells numbered 1 and upon the Faith Oil Corporation-O. F. Wencker farm more particularly described as 14.15 acres out of the B. W. Witcher Survey, more particularly described by metes and bounds on the reverse side hereof, in Gregg County, State of Texas, including the royalty interest and until further written notice you are authorized for your own account to receive oil therefrom into your possession or the possession of any person or corporation designated by you, giving credit as directed below:

Due to the great number of royalty owners and the small interests it is agreed that Simms Oil Company, at its option, shall not make payment for the runs to the credit of any interest until there has accumulated as much as $5.00, and in any event, payment shall not be made oftener than every three months.

Credit to—	Division of interest	P. O. address
Faith Oil Corporation	⅛ W. I.	c/o J. J. Perkins, Wichita Falls.
Fred P. Branson	⅛ W. I.	c/o Skirvin Hotel, Okla City, Okla.
Mrs. Mami (S. Hammonds	⅛ W. I.	623 E. 18th St., Okla City, Okla.

"Division of royalty interest omitted because immaterial," as per stipulation of counsel copied at page one hereof.

* * * * * * *

Simms Oil Company is hereby authorized until further notice to receive oil from said wells for purchase from the said parties severally the proportions named, subject to the following conditions:

First: That oil run in pursuance of this division order
60 shall become the property of Simms Oil Company as soon as the same is received into the custody of it or its designated agent.

Second: The oil received in pursuance of this division order shall be paid for to the party or parties entitled thereto according to the interest shown above, at the posted price of Sun Oil Company in the field where received, for the same kind and quality of oil on the day of the receipt thereof, payments to be made monthly by checks mailed to said party or parties at their respective addresses above set out.

Third: Oil shall be steamed when necessary to render it merchantable. A deduction of two percent (2%) from the oil received shall be made to cover evaporation, shrinkage, waste or other loss. The oil must be free from sand, dirt, water, emulsion or other sediment, and if found not to be such by the tests then in use by Simms Oil Company, may be rejected or at the option of Simms Oil Company may be accepted and when accepted Simms Oil Company shall be permitted to deduct the full percentage of sand, dirt, water emulsion and/or other sediment found to be contained in the oil. Corrections will be made for temperatures, deducting or allowing on a basis of one per cent (1%) for each 25 degrees Fahrenheit variation above or below 60 degrees Fahrenheit.

Fourth: The undersigned agrees to furnish Simms Oil Company with satisfactory abstracts and other evidence of title at any time on demand and in event of failure to so furnish such evidence of title, or in case of any adverse claim of title to furnish to Simms Oil Company upon demand a suitable and satisfactory bond executed by a surety company authorized to do business in Texas, indemnifying Simms Oil Company against such claim or claims and that Simms Oil Company may retain the purchase price
61 of the oil without interest until furnished such bond or until the dispute as to ownership is settled satisfactorily to said company.

Fifth: This agreement and division order shall become valid and binding on each and every owner above named as soon as signed by him or her, regardless of whether or not any of the other above named owners have so signed.

Effective with runs beginning seven o'clock A. M. Date of first runs.

Witnesses:

(There must be two witnesses to each signature.)

FAITH OIL CORPORATION,

By ---

President.

Attest:

Secretary.

Metes and Bounds Description of O. F. Wencker 14.15 Acre Farm

Situated in the County of Gregg, State of Texas, described as follows, to-wit:

"Detailed description omitted because immaterial", as per stipulation of counsel copied at page one hereof.

* * * * * * *

62 *Plaintiff's Exhibit 6-b*

(Being the same in words and figures as Plaintiff's Exhibit 6-a shown above.)

Plaintiff's Exhibit 6-c

Simms Oil Company

Division Order

JUNE 27TH, 1932.

To SIMMS OIL COMPANY:

The undersigned certify and guarantee that they are the legal owners of wells numbered 1 and up on the Faith Oil Corp.—J. C. Barrett Farm, more particularly described as South 140 acres out of the B. W. Witcher Survey, in Gregg County, State of Texas, including the royalty interest, and until further written notice you are authorized for your own account to receive oil therefrom into your possession or the possession of any person or corporation designated by you, giving credit as directed below:

Credit to—	Division of interest	P. O. address
Faith Oil Corporation	20/32 W. I.	Wichita Falls, Texas.
Mamie S. Hammonds and Fred P. Branson (One-half each)	8/32 W. I.	623 E. 18th St. Okla. City, Ok. Skirvin Hotel, Okla. City, Ok.

Until they receive the sum of $395,000.00, out of the J. C. Barrett and other leases.

63 Simms Oil Company is hereby authorized until further notice to receive oil from said wells for purchase from the said parties severally in the proportions named. subject to the following conditions:

First: That oil run in pursuance of this division order shall become the property of Simms Oil Company as soon as the same is received into the custody of it or its designated agent.

Second: The oil received in pursuance of this division order shall be paid for to the party or parties entitled thereto according to the division of interests shown above, at such price as Simms Oil Company is currently willing to pay for oil received from the above-described lease on the day of receipt thereof. Notices of your current price basis and any changes therein are to be addressed to the undersigned at the respective post office addresses shown above. Payments to be made monthly by checks mailed to said party or parties at their respective addressed above set out.

Third: Oil shall be steamed when necessary to render it merchantable. A deduction of two percent (2%) from the oil received shall be made to cover evaporation, shrinkage, waste, or other loss. The oil must be free from sand, dirt, water, emulsion, or other sedi-

ment, and if found not to be such by the tests then in use by Simms Oil Company, may be rejected or at the option of Simms Oil Company may be accepted and when accepted Simms Oil Company shall be permitted to deduct the full percentage of sand, dirt, water, emulsion, and/or other sediment found to be contained in the oil. Corrections will be made for temperature, deducting or allowing on a basis of one percent (1%) for each 25 degrees Fahrenheit variation above or below 60 degrees Fahrenheit.

Fourth: The undersigned agrees to furnish Simms Oil Com-
64 pany with satisfactory abstracts and other evidence of title at any time on demand and in event of failure to so furnish such evidence of title, or in case of any adverse claim of title, to furnish to Simms Oil Company upon demand a suitable and satisfactory bond executed by a surety company authorized to do business in Texas, indemnifying Simms Oil Company against such claim or claims", and that Simms Oil Company may retain the purchase price of the oil without interest until furnished such bond or until the dispute as to ownership is settled satisfactorily to said company.

Fifth: This agreement and division order shall become valid and binding on each and every owner above named as soon as signed by him or her, regardless of whether or not any of the other above named owners have so signed.

Effective with runs beginning seven o'clock A. M. date of First Runs.

(There must be two witnesses to each signature.)

[SEAL] FAITH OIL CORPORATION, INC.
W. J. GREEN, *President.*
MAMIE S. HAMMONDS.
O. O. HAMMONDS.
FRED P. BRANSON.

Attest:

MRS. L. W. BREWSTER, *Secy.*
D. D. FORD.
DR. N. DEA GRIFFITH.
DR. L. RIPPETS.
D. D. FORD.

The WITNESS. These division orders, as shown in Plaintiff's Exhibits 6 a, b, c, are the customary orders used in the oil business.

65 We have connections with several pipe line companies down there, and those connections have changed from time to time; there were some changes made in the pipe lines running this oil, but the form of the division orders were always the same, and the division of the oil was always the same.

I, together with the same associates that were interested in the Branson and Hammonds property, had a property which was acquired from E. H. Brawley in the same territory. This instrument which you hand me is the oil and gas lease acquired from Mr. Brawley, for which we paid $22,500.00 cash bonus.

Mr. WEEKS. We offer it in evidence.

Mr. BACKSTROM. We object to this. There is no allegation in the petition relative to this transaction. It seems to me that it is not proper as evidence in this proceeding at all. It does not support any allegation of the petition.

The COURT. It was stated by Mr. Weeks in his opening statement, the Brawley transaction.

Mr. WEEKS. He may be correct about that. There is a few hundred dollars that came from the Brawley lease. I would like leave to cover that, is the same sort of transactions as the ones we have dealt with in our petition. This nine thousand and some odd thousand dollar income from these various properties, I think six or seven hundred dollars came from the Brawley properties.

The WITNESS. The Brawley property only has one well.

66 Mr. POTTER. We have no objection to the amendment, but we think it ought to be included.

The COURT. All right.

Mr. WEEKS. May I proceed on that theory, and sometime during the day the allegations will be made and filed,

Mr. POTTER. That is all right.

(Said instrument marked "Plaintiff's Exhibit 7" and reading as follows:)

Plaintiff's Exhibit 7

Oil & Gas Lease

Dated October 21, 1931

Filed November 2, 1931

Recorded Vol. 14, pg. 397

Upshur Co. O & G Rec.

E. H. Brawley to W. J. Green.

Agreement made and entered into the 21st day of October

67 1931, by and between E. H. Brawley and wife, Cora Brawley, of Longview, Gregg County, Texas, hereinafter called lessor (whether one or more), and W. J. Green, hereinafter called lessee:

Witnesseth: That the said lessor for and in consideration of Ten dollars, cash in hand paid, the receipt of which is hereby acknowledged, and of the covenants and agreements hereinafter contained on the part of lessee to be paid, kept and performed, have granted, demised, leased and let and by these presents do grant, lease and let unto the said lessee for the sole and only purpose of mining and operating for oil and gas and of laying pipe lines and of building tanks, power stations and structures thereon to produce, save and take care of said products, all those certain tracts of land situated in the County of Upshur, State of Texas, and containing 450 acres more or less, described as follows, to-wit:

"Detailed description omitted because immaterial", as per stipulation of counsel copied at page one hereof.

* * * * * * *

It is understood and agreed that as a part of the consideration for the execution of this lease, lessee is to pay to lessors an oil payment of forty-five thousand dollars ($45,000.00) said oil payment to be paid out of one-fourth of seven-eighths working interest.

E. H. BRAWLEY.

It is agreed that this lease shall remain in force for a term of ten years from date, and as long thereafter as oil, gas or either of them, is produced from said land by the lessee.

68 In consideration of the premises the said lessee covenants and agrees:

1st. To deliver to the credit of the lessor, free of cost, in the pipe line to which lessee may connect his wells, the equal one-eighth part of all oil produced and saved from the leased premises.

2nd. To pay to lessor, as royalty for gas from each well where gas only is found, while the same is being sold or used off of the premises, one-eighth of the market price at the wells of the amount so sold or used, the lessor to have gas free of charge from any well on the leased premises for all stoves and inside lights in the principal dwelling house on said land by making lessor's own connections with the well at lessor's own risk and expense.

3rd. To pay to lessor as royalty for gas produced from any oil well and used by lessee for the manufacture of gasoline, one-eighth of the market value of such gas. If such gas is sold by lessee, then lessee agrees to pay lessor, as royalty one-eighth of the market price at the wells of the amount sold.

If no well be commenced on said land on or before the 21st day of October, 1932, this lease shall terminate as to both parties, unless the lessee on or before that date shall pay or tender to the lessor or to the lessor's credit in the First National Bank at Longview, Texas, or its successors, which shall continue as the depository regardless of changes in the ownership of said land, the sum of four hundred fifty & No/100 dollars, which shall operate as a rental and cover the privilege of deferring the commencement of a well for twelve months from said date. In like manner and upon like payments or tenders the commencement of a well may be further deferred for like periods of the same number of months successively.

69 And it is understood and agreed that the consideration first recited herein, the down payment covers not only the privilege granted to the date when said rental is payable as aforesaid, but also the lessee's option of extending that period as aforesaid and any and all other rights conferred.

Should the first well drilled on the above described land be a dry hole, then, and in that event, if a second well is not commenced on said land within twelve months from the expiration of the last rental period which rental has been paid, this lease shall terminate

as to both parties, unless the lessee on or before the expiration of said twelve months shall resume the payment of rentals in the same amount and in the same manner as hereinbefore provided. And it is agreed that upon the resumption of the payment of rentals, as above provided, that the last preceding paragraph hereof, governing the payment of rentals and the effect thereof, shall continue in force just as though there had been no interruption in the rental payments.

If at the expiration of ten years from the date of this lease, oil or gas is not being produced on the leased premises, but lessee is then engaged in drilling for oil or gas, then this lease shall continue in force so long as drilling operations are being continuously prosecuted on the leased premises; and drilling operations shall be considered to be continuously prosecuted if not more than sixty (60) days shall elapse between the completion or abandonment of one well and the beginning of operations for the drilling of a subsequent well. If oil or gas shall be discovered and produced in paying quantities from any such well or wells drilled or being drilled at or after the lapse of ten years, this lease shall continue in force so long as oil or gas shall be produced from the leased premises.

It is specially agreed that in the event that oil or gas is
70 produced from said premises and said production shall for any reason cease or terminate, lessee shall have the right at any time within ninety (90) days from the cessation of such production to resume drilling operations in the effort to make said leased premises again product oil or gas, in which event this lease shall remain in force so long as such operations are continuously prosecuted, as defined in the preceding paragraph, and if they result in production of oil or gas, so long thereafter as oil or gas is produced in paying quantities from the premises.

If said lessor owns a less interest in the above described land than the entire and undivided fee simple estate therein, then the royalties and rentals herein provided for shall be paid the said lessor only in proposition which lessor's interest bears to the whole and undivided fee.

Lessee shall have the right to use, free of cost, gas, oil and water produced on said land for all operations thereon except from water wells of lessor. When requested by lessor, lessee shall bury its pipe line below plow depth. No well shall be drilled nearer than 200 feet to the house or born now on said premises without the written consent of the lessor; lessee shall pay for damages caused by all operations to growing crops on said land. Lessee shall have the right at any time to remove all machinery and fixtures placed on said premises, including the right to draw and remove casing.

If the estate of either party hereto is assigned and the privilege of assigning in whole or in part is expressly allowed, the covenants hereof shall extend to their heirs, executors, administrators, successors or assigns, but no change in the ownership of the land or

assignment of rentals or royalties shall be binding on the lessee until after the lessee has been furnished with a written transfer or assignment or a true copy thereof; and it is hereby agreed in the event this lease shall be assigned as to a part or parts of the above described lands and the assignee or assignees of such part or parts shall fail or make default in the payment of the proportionate part of the rents due from him or them, such default shall not operate to defeat or affect this lease in so far as it covers a part or parts of said lands upon which the said lessee or any assignee thereof shall make due payment of said rental.

71

Lessee shall have the exclusive right to build, operate, and maintain pits, reservoirs, pickup stations and plants for the purpose of picking up and conserving the waste oil that follows down the creeks, ravines, and across the land embraced in this lease, whether said oil is produced from lands covered by this lease or other lands and lessor shall be entitled to receive the royalty hereinbefore reserved on all such oil so saved.

In case of cancellation or termination of this lease for any cause, lessee shall have the right to retain under the terms hereof twenty (20) acres of land around each oil or gas well producing, being worked on, or drilling hereunder (as long as such operations are continued in good faith) such tract to be designated by lessee in as near a square form as practicable.

In the event lessor considers that lessee has not complied with all its obligations hereunder, both expressed and implied, before production has been secured or after production has been secured, lessor shall notify lessee, in writing, setting out specifically in what respects lessee has breached this contract. Lessee shall then have sixty (60) days after receipt of said notice within which to meet or commence to meet all or any part of the breaches alleged by lessor. The service of said notice shall be precedent to the bringing of any action by lessor on said lease for any cause, and no such action shall be brought until the lapse of sixty (60) days after service of such notice on lessee. Neither the service of said notice nor the doing of any acts by lessee aimed to meet all or any of the alleged breaches shall be deemed an admission or presumption that lessee has failed to perform all of its obligations hereunder.

72

Title to the minerals vested in grantee under this grant shall not end or revert to grantor until there is a complete, absolute and intentional abandonment by grantee of each and all of the purposes, expressed or implied, of this grant and every part and parcel of the premises described in this grant.

Lessor hereby warrants and agrees to defend the title to the lands herein described and agrees that the lessee shall have the right at any time to redeem for lessor, by payment, any mortgage, taxes, or other liens on the above described lands, in the event of default of payment by lessor, and be subrogated to the rights of the holder

thereof, and lessor hereby agrees that any such payment made by the lessee for the lessor shall be deducted from any amounts of money which may become due the lessor under the terms of this lease.

The $45,000.00 oil payment above referred to is not a personal obligation, but only to be paid out of one-fourth of seventh-eighths of the oil, gas, if and when produced.

E. H. BRAWLEY.

In testimony whereof, we sign this the 21st day of Oct. 1931.

E. H. BRAWLEY.
CORA BRAWLEY.

THE STATE OF TEXAS,
County of Upshur.

Before Me, the undersigned, a Notary Public in and for said
73 County and State on this day personally appeared E. H. Brawley and Cora Brawley, his wife, both known to me to be the persons whose names are subscribed to the foregoing instrument and acknowledged to me that they each executed the same for the purposes and consideration therein expressed, and the said Cora Brawley, wife of the said E. H. Brawley, having been examined by me privily and apart from her husband and having the same fully explained to her, she, the said Cora Brawley acknowledged such instrument to be her act and deed, and she declared that she had willingly signed the same for the purposes and consideration therein expressed, and that she did not wish to retract it.

Given Under My Hand And Seal Of Office this the 21st day of October, A. D. 1931.

[SEAL] ERNESTINE BOBO,
Notary Public in and for Upshur Co., Texas.

The WITNESS. The Faith Oil Company and myself were interested with Mr. Green in this lease in the same proportion as in the other lease. There was no production on that property when the lease was made. There was one well drilled on that in the extreme southeast corner, the lease being on the west side of the East Texas field, and it is producing oil. There have been two other wells drilled and both of them were dry. I have continued to own my interest through 1933 in that property, there has been no change. The production from that property was handled, with reference to its disposition and sale, in the same way as that from the Branson and Hammonds property, one-fourth of seven-eighths going to Mr. Brawley, in addition to his one eighth, and the usual form of division order. This instrument which you hand me is one of the divison orders that was used on the Brawley property.

Mr. WEEKS. We offer the instrument in evidence.

74 (Said instrument marked "Plaintiff's Exhibit No. 8" and reading as follows:)

Plaintiff's Exhibit 8

Humble Oil & Refining Company

Division Order No. 5074

Effective y a. m., August 12, 1932

To HUMBLE OIL & REFINING CO.,
Houston, Texas:

The undersigned certify and guarantee that they are the owners of the oil, including royalty interest, produced from wells, No. 1 and up, on the E. H. Brawley Farm or lease, in _____ Oil Field in Upshur County, Texas, which farm or lease is described as follows:

All that certain tract or parcel of land situated in Upshur County, Texas, being 180 acres of land on the H. R. Survey of Jackson Crouch described as follows, to-wit:

Beginning at the SE. corner of a 320-acre survey made for W. O. Barker as a pre-emption; thence south 428 vrs.; thence W. 21 vrs. corner; thence S. 428 vrs. to a stake pine brs. N. 50 1/2 E. 5 8/10 vrs. a pine brs. S. 38 W. 8 9/10; thence west 1323 vrs. a stake a pine brs. S. 70 W. 4 3/10 vrs. a pine brs. S. 25 E. 3 vrs.; thence north 874 vrs. a corner; thence east 14 vrs. corner at 1523 vrs. to beginning, containing 180 acres of land, more or less.

Until further written notice, you are authorized, for your own account, to receive such oil into your own possession or the possession of any person or corporation designated by you, same to be run and measured in accordance with the customary pipe line rules and regulations, including adjustments and deductions pro-
75 vided for by the rules of the Texas Railroad Commission, such oil to be credited as follows:

Credit to—	Division of interest	Post office address
Farmers & Merchants National Bank of Gilmer	⅞	Gilmer, Texas.
(The above interest subject to the payment to E. H. Brawley and wife of $45,000.00 out of a ¼ of ⅞ part of production.)		
E. H. Brawley & Wife, Cora Brawley	⅛	

For all oil run and purchased under this division order subsequent to 7 A. M. August 17, 1931, until further notice, or until a field price is posted as hereinafter provided, Humble Oil & Refining Company will pay what it interprets to be the going price for East Texas crude oil sold from this field during the regular settlement period during which the oil is run, exclusive of oil sold under contracts made prior to 7 A. M. June 3, 1931.

Humble Oil & Refining Company does not have a posted price for oil from this field at this time, but if and when Humble Oil & Refining Company does post a regular price for oil in this field, from

such time and thereafter, until further notice, such regular posted field price shall control and shall govern purchases thereafter made under this division order.

The oil run hereunder shall on the terms herein contained become the property of Humble Oil & Refining Company immediately upon being received into the possession of said Company or its designated agent, and said Company agrees to receive and pay for such oil to the respective owners according to the division of interest hereinabove indicated at its posted per-barrel (42 gallons) field price for similar crude in the field where received prevailing on the date of each respective run, settlements, and payments to be made
76 monthly by check of Humble Oil & Refining Company mailed to the respective parties at the addresses above given.

Each undersigned hereby warrants and guarantees the title to the oil credited to such undersigned owner according to the division of interest hereinabove indicated, as well as all interest hereafter acquired, and agrees to furnish abstract of title, and in case of any adverse claim of title to such oil or any part thereof, or to the land from which such oil is produced, to furnish Humble Oil & Refining Company satisfactory indemnity bond against such adverse claim or claims and to authorize Humble Oil & Refining Company to retain the purchase price without any obligation to pay interest on the amount so withheld until such bond shall be furnished or until dispute as to the ownership is settled.

FARMERS & MERCHANTS
NATIONAL BANK OF GILMER,
By H. J. CHILDRESS, *President.*

Attest:

C. T. CROSBY, *Cashier.*
FAITH OIL CORPORATION.
By W. J. GREEN, *President.*
C. T. CROSBY,
E. H. BRAWLEY,
CORA BRAWLEY.

Witnesses.:
Attest:

----------,
Secretary.
J. P. RAY,
J. M. LOCKHART,
L. S. BRAWLEY.

Accepted and agreed to:

HUMBLE OIL & REFINING CO.,
By ----------

77 The WITNESS. That division order provides for our portion of the oil to go to the Farmers and Merchants National Bank, it went to them as a pledge for an indebtedness, but the proceeds were for our account.

My experience has been, in respect to transactions of this character, that we could not have collected for any portion of the oil applicable to the oil payment under any consideration, except by the written consent of the holders of the oil payment given to the pipe line companies running the oil.

I am quite sure that the Branson and Hammonds Oil payment will be paid out within two and a half years, from this time; that statement is based upon the geology and experience we have had over in the East Texas field. Approximately one-half of that $395,000.00 has been paid at this time. In respect to the Brawley payment, there is no chance for that to pay out. We only have one well, and I don't think we will ever drill any more, because this well is making a large amount of water. It will probably produce, from the best information available, two or three years more—so that the Brawley payment is the same as a perpetual royalty.

In making my tax returns for the year 1933, this fraction of the oil and its proceeds which went to Branson and Hammonds in the one instance and Brawley in the other, was not included by me as part of my income. It was not included in our original tax returns, but was set up by the revenue agent when he audited our returns at a later date.

I owned an interest in some property in Moore County, West Texas, known as the Ozier Ranch. I bought one-third interest in the west half of the Ozier Ranch, consisting of about fifty-three hundred acres, from Will O'Brian. I agreed to pay him ten thousand dollars for that third interest and take it subject to some sixty thousand dollars original first lien vendor lien notes against the en-
78 tire Ozier Ranch, consisting of a little over ten thousand acres. This instrument which you hand me is a copy of the deed by which I acquired that one-third interest.

Mr. WEEKS. We offer the deed in evidence.

(Said instrument marked "Plaintiff's Exhibit No. 9" and reading as follows:)

Plaintiff's Exhibit No. 9

THE STATE OF TEXAS,
County of Potter.

Know All Men By These Presents: That I, W. O'Brien and wife, Exie E. O'Brien, of the County of Potter, State of Texas, for and in consideration of the sum of Ten Thousand ($10,000.00) cash paid to us in hand paid by J. J. Perkins, the receipt whereof is hereby acknowledged, have granted, sold, remised, released and forever quit claimed and by these presents do grant, sell, remise, release and forever quit claim unto the said J. J. Perkins, his heirs and assigns all our right, title and interest in and to that certain lot, tract or parcel of land described as follows:

A one-third undivided interest in all of Section 53, 54 and 55, in Block 47, H. & T. C. Ry. Co., each containing 640 acres of land; all

of Sections 50, 51, 76 and 79 in Block G. & M. 3, Sections 50, 51 and 76 and 79 in Blocks G. & M. 3, Sections 50, 51, and 76, containing 640 acres of land, and Section 79 containing 282.2 acres of land, all of Section 77 in Block G. & M. 3, containing 426.2 acres of land, same being all of said Sections deeded to W. R. Ozier by R. B. Masterson.

79 Section Number (10) in Block B 12, D. & R. P. Ry. Co., containing 640 acres of land, Section number 48, in Block G. & M. 3, containing 192 acres, and being all of said section deeded to W. R. Ozier by R. B. Masterson.

This deed is intended to convey and does convey a one-third interest in all of the lands purchased by W. O'Brien when sold by the Sheriff of Moore County, Texas, on the 7th day of August 1923, and for further descriptions of said above described land, reference is made to said sale.

To Have And To Hold the above described premises together with all and singular the rights and appurtenances thereto in anywise belonging unto the said J. J. Perkins, his heirs and assigns forever, so that neither the vendor herein nor their heirs, nor any other person or persons for themselves or in their name or behalf, shall or will hereafter claim or demand any right or title to the aforesaid premises or any part thereof, but they and every one of them by these presents shall be excluded and forever barred.

Witness our hand this 8th day of November, A. D. 1925.

W. O'Brien.
Exie E. O'Brien.

The State of Texas,
County of Potter.

Before Me a Notary Public in and for County of Potter of the County in the State of Texas on this day personally appeared W. O'Brien and Exie E. O'Brien, his wife, both known to me (or proved to me on the oath of ____) to be the persons whose names are subscribed to the foregoing instrument and acknowledged to me that they each executed the same for the purposes and consideration therein expressed. And the said Exie E. O'Brien, wife of the said W.

80 O'Brien, having been examined by me privily and apart from her husband and having the same fully explained to her, she, the said Exie E. O'Brien, acknowledged such instrument to be her act and deed and declared that she had willing signed the same for the purposes and consideration therein expressed, and that she did not wish to retract it.

Given Under My Hand And Seal Of Office this 8th day of November, A. D. 1925.

[seal] H. V. Knupp.

Filed December 15, 1925, at 9 o'clock A. M.

Recorded January 2, 1926—Volume 27, page 458.

The Witness. I will outline briefly the circumstances under which I acquired that property; Mr. O'Brien, of Amarillo, who is a very close personal friend of mine, came down to Wichita Falls and told

me that he had acquired, through a foreclosure of a deed of trust, that was given to his bank, the National Bank of Commerce of Amarillo, what he termed the west half of the Ozier Ranch, and that it was subject to the original purchase money notes given for the purchase of the entire ranch, by Mr. Ozier. The notes at that time being held by Mr. Masterson, and being past due, he said that he felt that an effort was being made for those notes to be foreclosed on in such way as to wipe out his interests. He asked me if I would not advance the money to take up the original purchase money notes, and file suit for a foreclosure of that lien, marshaling the assets by selling the East half of the ranch, and if that sold for enough to pay, it would have the effect of wiping out the lien on the entire ranch, if it did not sell for enough, then they would sell the west half. I told him I would, and I gave him a check at that time for the $59,000.00, and he took it back to Amarillo and took up the notes from Mr.
81 Masterson and immediately turned them over to Judge Reeder to file suit to foreclose the lien.

This deed from Mr. O'Brien to me is dated November 8, 1925. This other transaction in respect to these notes held by Masterson was the—the last of January, 1924 is when I made the trade and entered into a contract with Mr. O'Brien, but I did not take title; that is also when I paid off the notes, in January, 1924, but I did not take title until after the entire matter was cleaned up through the Courts. This suit that was instituted by me on the Masterson note, was prosecuted to a conclusion, and the Court ordered that the east half of the Ozier Ranch be sold to satisfy a judgment, which was with interest and attorney's fees, nearly seventy thousand dollars, and the land was sold under execution in September, 1924. However, the judgment was appealed from and went on finally to the Supreme Court of Texas, but the land was sold under the execution issued from that judgment, September, 1924. I think the land brought ten dollars more than the entire amount of the judgment. Jim Shelton, Mr. Ozier's son-in-law, bought it.

The agreement I made with Mr. O'Brien, in January, 1924, was that I was to take a one-third interest in the west half, Mr. O'Brien retain one-third interest, and Mr. Lee Bivins one-third interest. In 1933 Mr. O'Brien and I sold our two-thirds interest in the west half of all the mineral on that ranch to the Amarillo Gas Company, the Bivins estate did not join in the sale. This instrument which you hand me is the instrument by which the minerals were conveyed. There was a small portion of the mineral outstanding in three sections when we bought the ranch, being owned by Mr. Kay and others, and they joined in the sale at the same time we sold ours.

Mr. WEEKS. We offer the instrument in evidence.

82 (Said instrument marked "Plaintiff's Exhibit No. 10" and reading as follows:)

Plaintiff's Exhibit No. 10

STATE OF TEXAS,
Counties of Moore & Potter:

Know All Men By These Presents: That, Whereas, W. O'Brien, W. L. Mathers and J. J. Perkins own an undivided 2/3rds interest in the mineral estate in and to the land hereinafter described as Tract No. 1, and an undivided 5/12ths interest in the mineral estate in and to the tract hereinafter described as Tract No. 2 and own an undivided 2/3rds interest in the surface estate in and to all of the land hereinafter described, and A. W. Kay, Finley Scruggs Jr. and C. B. Dodge own an undivided 12/40ths interest in the mineral estate in and to the lands hereinafter described as Tract No. 2.

Now, Therefore, Know All Men By These Presents: That we, W. O'Brien and W. L. Mathers, of Potter County, Texas, J. J. Perkins of Wichita County, Texas, A. W. Kay of Young County, Texas, Finley Scruggs, Jr., of Smith County, Texas, and C. B. Dodge of Saline County, Kansas, for and in consideration of the sum of $45,686.66 cash in hand paid by Amarillo Oil Company a corporation, receipt of which sum is hereby acknowledged, have granted, sold, assigned, conveyed and delivered and by these presents do grant, sell, assign, convey and deliver unto the said Amarillo Oil Company, a corporation, organized and existing under the laws of the State of Texas, an undivided 2/3rds interest in the oil, gas and other minerals in, under and that may be produced from the land hereinafter described as Tract No. 1 situated in Moore and Potter Counties, Texas, to-wit:

Tract No. 1:

All of Sections 50, 51, 76, and 79 in Block No. G & M 3,
83 said sections 50, 51, and 76 containing 640 acres each, and section 69 containing 282.3 acres of land; all of section 10, Block B-12, D. & P. Ry. Co. survey, containing 640 acres; all of section 77, Block G & M 3, containing 426.5 acres, and the east part of section 48, Block G & M 3, containing 192.2 acres. Reference is here made to the deed records of Moore County, Texas, for an exact description of that portion of Section 48 herein conveyed.

and an undivided 86/120ths interest in the oil, gas, and other minerals in, under, and that may be produced from the land hereinafter described as Tract No. 2, situated in Moore and Potter Counties, Texas, to-wit:

Tract No. 2:

All of sections 53, 54, and 55, in Block No. 47, H. & T. C. Ry. Co. Survey, each containing 640 acres;

All of said tracts containing in the aggregate of 5,381 acres, more or less.

together with the full right of ingress and egress at all times for the purpose of mining and operating for oil or gas and other minerals,

and of laying pipe lines and the erecting of telegraph and telephone lines, and of building tanks, power stations, and structures, and notwithstanding the above enumeration, the full right to go upon said lands and use the same for any purpose reasonably necessary or incident to the operations upon said lands for the purpose of mining, drilling, and exploring the same for oil, gas, and other minerals, and removing the same therefrom. The grantee herein, its successors and assigns, shall have the right to use, free of cost, water produced on said lands for its operations thereon, except water from wells or tanks of the grantors herein.

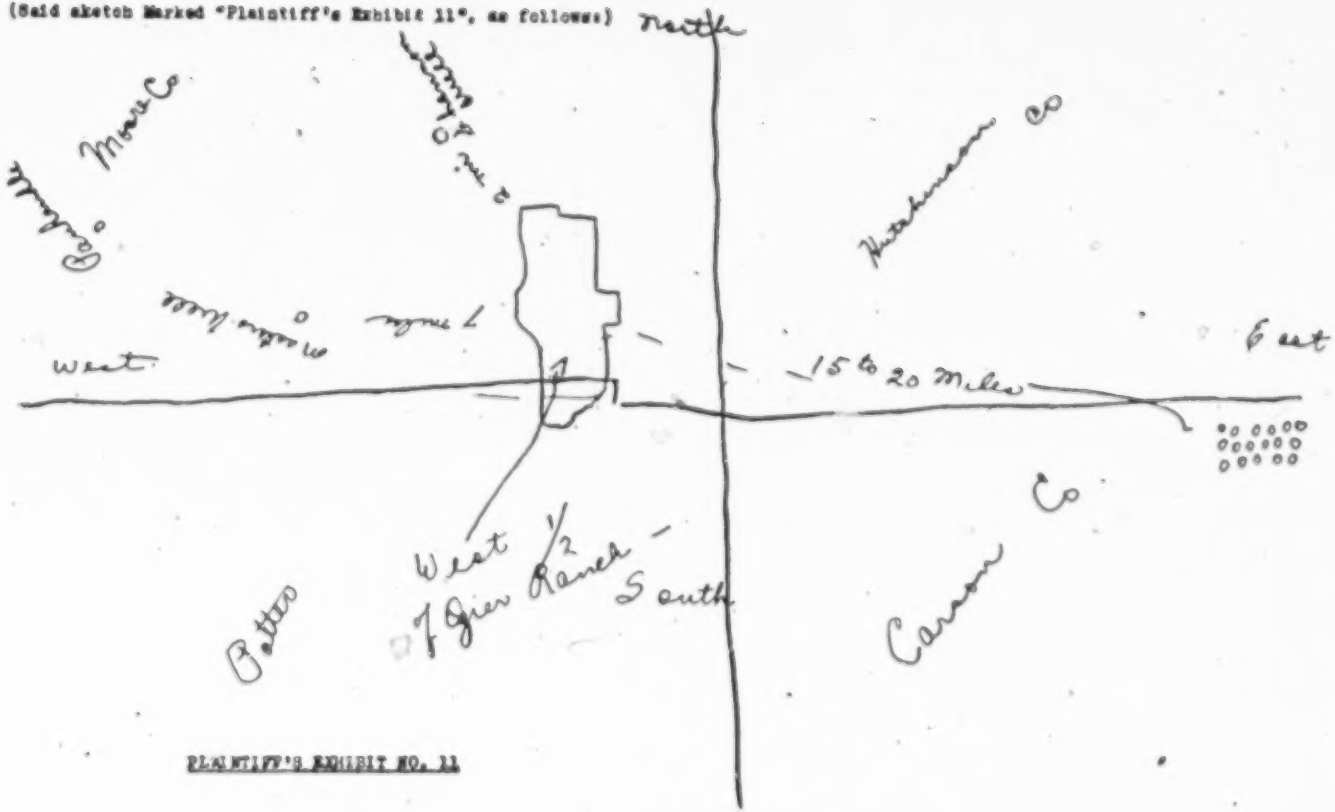
This mineral conveyance shall cover and include all lands
84 owned by the grantors herein as excess acreage in or contiguous to the surveys or descriptions as above set forth, and shall cover and include all of the mineral interest and estate that the grantors herein have in and to the surveys hereinabove described, whether the description hereinabove contained is absolutely accurate or not.

Said land is now under an oil and gas lease executed in favor of Amarillo Oil Company dated May 23, 1928, and recorded in Volume 37, page 368, of the Deed Records of Moore County, Texas, reference to which is here made, and it is agreed and understood that this sale is made subject to the terms of such lease, but covers and includes 2/3rds as to Tract No. 1 and 86/120ths as to Tract No. 2 of the oil royalty and gas rental and royalty due and to be paid under the terms of said lease.

It is understood and agreed that 2/3rds as to Tract No. 1 and 86/120ths as to Tract No. 2 of the money rentals which may be paid to extend the terms within which a well may be begun under the terms of such lease is to be paid to the grantee herein, its successors and assigns, and in the event that the above described lease becomes canceled or forfeited or terminates for any cause whatsoever, that then, and in that event, 2/3rds as to Tract No. 1 and 86/120ths as to Tract No. 2 of the mineral estate and future rentals, whether delay rentals or otherwise, and bonuses on said land for oil, gas, or other mineral privileges shall be owned by the grantee herein, its successors and assigns.

To Have And To Hold the above described property, together with all and singular the rights and appurtenances thereto in any wise belonging unto the said Amarillo Oil Company, its successors and assigns, forever, and the grantors herein do hereby bind themselves, their heirs, executors, and administrators, to warrant and for-
85 ever defend all and singular the property herein conveyed unto the said grantee herein, its successors and assigns, against every person whomsoever claiming or to claim the same, or any part thereof. It is understood, however, that this warranty as to A. W. Kay, Finley Scruggs, Jr., and C. B. Dodge shall be and is limited to the interest herein conveyed by them, as hereinabove set out, and the warranty of the other grantors herein shall extend to the remainder of the property herein conveyed, as hereinabove set out.

(Said sketch Marked "Plaintiff's Exhibit 11", as follows)



PLAINTIFF'S EXHIBIT NO. 11

"Acknowledgments and recording data omitted because immaterial", as per stipulation of counsel copied at page one hereof.

* * * * * * *

The WITNESS. Prior to that time I had been operating in the oil business in the Panhandle in the neighborhood of this Moore County property. I owned a fourth interest in the Dial Ranch in Hutchinson County, about fifteen miles East of the Ozier Ranch. I think that is all the properties I had at that time up there. The Dial Ranch only had one little well on it, however, we bought the Dial ranch as an oil possibility when we bought it. I was familiar with the course of oil and gas development in the Panhandle area at the time of this transaction with Mr. O'Brien. As to the prospects on this Ozier Ranch, the part of it which I acquired an interest in, as to producing gas and oil on the date of the deed from Mr. O'Brien to me in 1925, I will state there had been drilled three gas wells to the west and northwest of the Ozier Ranch from two to five miles; and there had been some production found on the north line of the Burnett Ranch on the north line of Carson County, some fifteen or eighteen miles east and a little south of the Ozier Ranch. So that the Ozier Ranch was in between the two gas wells and the oil as
86 it had been found. And the oil and gas possibilities is the only reason that I would have considered buying the Ozier Ranch at all. I had no interest in it other than from an oil-and-gas standpoint. At the time I bought this property from Mr. O'Brien I felt quite certain that it would produce gas, and we were hoping it would produce oil, and from that standpoint I felt that it would be a good investment to buy it, so I bought it.

I have a map of that territory out there, which covers several counties in the Panhandle.

I would like to correct one statement before going into that; you asked me if I had any other oil interest in the Panhandle; I had a small interest in the Shamrock well, being one of the wells drilled on the west or northwest of the Ozier Ranch, three or four years prior to the time I made this trade, and I still owned that interest at the time I bought the Ozier Ranch propery.

This map here correctly reflects the location of this land with respect to the various counties and their boundaries up there.

I have prepared a sketch which correctly shows, with substantial correctness, the location of this Ozier Ranch, the part of it in which I was interested, and the county lines up there. This instrument which you now hand me is the one I prepared.

Mr. WEEKS. We offer it in evidence.

88 The WITNESS. This irregular shaped piece of land here is the Ozier Ranch, that is the west half of it; that lies principally in the south east corner of Moore County, and extends into the north east corner of Potter County.

In 1925, when I bought this interest in the Ozier Ranch, there was some develop on the east.

Mr. BACKSTROM. He acquired the ranch in 1924, I think it is immaterial as to what was there in 1925.

The COURT. That is the way I view it.

Mr. WEEKS. The deed is dated in 1925.

The COURT. He has said that it was 1924, you had to refresh his memory.

Mr. WEEKS. Well, on the west half was 1924, his deed from Mr. O'Brien was dated November 8, 1925.

Mr. BACKSTROM. He alleged in his petition in 1924, and we admitted that.

Mr. WEEKS. Well, then, I will confine our testimony to that time.

The WITNESS. As to the condition existing in 1924, at the time Mr. O'Brien first came to me about the matter, I will state; at the time I made this contract with Mr. O'Brien in January 1924, there
89 was one small well on the Dial Ranch, it is north of the Canadian River in Hutchinson County, about twenty miles east and a little north of the Ozier Ranch property. There were a substantial number of wells on the north line of the Burnett Ranch, along the north line of Carson County, about twenty miles east and a little south of the Ozier Ranch. Some of those wells were oil wells and some of them gas wells. At the time I bought the Ozier Ranch, there had been a well drilled by the Shamrock Oil and Gas Company in which I had an interest, completed in May 1922, and made forty million feet of gas. That was on the Sneed Ranch on Section 42, T. & N. O. R. R. Company survey, Block 6, T. That was about two or two and a half miles northwest of the north line of the Ozier Ranch. Then some seven miles due west of the Ozier Ranch was the Masterson Oil and Gas Well, which was completed September 30, 1920. I, likewise, had an interest in that well. Then there was completed in November 1921, about twelve miles west of the Ozier Ranch, a well by the Panhandle Refining Company on the Thompson Ranch. This well was on Section 24, E. L. & R. R. Co. Survey, Block 26. I have marked those wells upon the sketch, Plaintiff's Exhibit No. 11, which has been offered in evidence.

I have had rather extensive experience in trading in land in this particular west Texas territory, I have had rather extensive dealings in land all over the entire Panhandle territory, for a period of perhaps twenty-five years. When I say extensive, I mean, I have bought and sold seventy-five to one hundred thousand acres of land, in perhaps fifty or one hundred different tracts over the panhandle. Previous to this time, I had acquired an interest in the Dial Ranch in 1922, which was eleven thousand acres, with a consideration of about $100,000.00. The other transactions I have spoken of, were in substantial amounts, I would imagine the entire consideration would be in excess of half a million dollars, or probably a million dollars.

90 This Ozier Ranch was rough pasture land, there was very little of the land that should have been put into cultivation. I had no interest in it, except from a mineral standpoint, when I

bought it, aside from the mineral in the land I would not have considered it, because it had no value to me from any standpoint except as to minerals. In my opinion the value of this property, that is, the cash market value at the time I made this trade with Mr. O'Brien, disregarding any mineral or oil or gas value which the property might have, I would not value it over $3.00 per acre as a maximum. I would say the value of the east and west half was approximately the same—I think that is true with reference to both the mineral and the surface value, that is, one is as valuable as the other, from a mineral standpoint, at that time.

Since I disposed of the minerals in the west half of the Ozier Ranch, I have disposed of the fee, for which I received $3.75 per acre, with $1.00 per acre in cash and the balance in one, two, and three years.

Q. What, in your opinion, is a fair apportionment between the value of the minerals in the west half of the Ozier Ranch at the date you acquired it, and the value of the surface?

Mr. BACKSTROM. We think that is objectionable. I think that is calling for a legal conclusion of the witness, to testify what the values were. What is a fair apportionment, I don't think is a proper opinion of the witness. I think that is a matter for Your Honor to determine, as a matter of law.

The COURT. I don't know about it being a matter of law, but I think it is probably for the determination of the fact finder; but the fact finder has to have some facts upon which to find. Here it is alleged mineral sale, an alleged sale of the realty outside of
91 the mineral, the fee, as it is called already in evidence, being unsatisfied with that the plaintiff offers to testify what is his opinion as to a fair apportionment.

Mr. WEEKS. It seems to me that the question is substantially the same as if we were attempting to determine how much of the total value of the piece of property is represented by the buildings and represented by the lot itself. Certainly a man would have to qualify to express an opinion; I think he should testify as to that; and just as easily and properly, it seems to me, an apportionment of the value of the fee and the surface can be made by witness knowing the property and otherwise qualified.

The COURT. You don't think the selling price is sufficient indication of apportionment?

Mr. WEEKS. Of course, the selling price of the surface in 1936 is quite remote from this acquisition, beginning in 1924 and consummated in 1925.

The COURT. In view of the objection, couldn't you figure it around and make it a little less remote?

The WITNESS. At the time I bought the land, I regarded the mineral as being worth perhaps three times as much as the surface, and I don't think there has been any change of any consequence since that time. During the time of our ownership we attempted to lease this

land for grazing purposes, but we received very little revenue from it. I was not in the ranching business, but I would say a fair grazing revenue for it would be about fifteen or twenty cents per acre.

The east and west half of this Ozier Ranch contained approx-
92 imately the same number of acres; there may have been two or three hundred more acres in one side than the other; there was supposed to be between ten and eleven thousand acres in the whole ranch, and there was five thousand three hundred and eighty-one acres in the west half.

Going back to the East Texas matters, we never received any portion of the money that was to be applied on the oil payments, and could not have received any portion of it except by the written consent of the owners of the payment—the money belonged to them; it did not belong to us.

I have my 1933 tax return available—I have both of my returns. Both of those returns report ordinary income and items of capital gain, the Ozier Ranch proposition being reported as a capital gain item; and the East Texas proposition coming within the ordinary income as I reported it.

Mr. WEEKS. There are some formal matters that we are in agreement about, and at this time we will not encumber the record with matters of that sort.

Cross-examination by Mr. POTTER:

The contract for the purchase of the land in Moore County was made in 1924; I was to receive one-third interest in five thousand three hundred and eighty-one acres, subject, of course, to the outstanding indebtedness against the entire ranch. As the matter terminated that indebtedness was wiped out by a foreclosure proceeding and a sale of half the ranch—that is, the east half. At the time I made the contract there was an indebtedness on it, but it was wiped out through the Court proceeding. The execution of the deed was only a formality carrying out the contract made in January 1924. I paid $10,000.00 for the one-third undivided interest in the west
93 half. I sold the surface rights in the land for $3.75, amounting to about $6,500.00. As to the value of that character of land, just as a surface proposition, I would say there has been little change in the value since the time I bought it, because it could not be used for anything except grazing purposes. I would assume the value in 1924 is about the same as it was in 1936.

I paid approximately $5.50 for this land in 1924, and sold it for $3.75 on terms. I do not think the value of the mineral rights was the difference between what I paid for it and what I sold the surface rights for, because I took the hazard of having to pay more than as much more than that for the land, that is, than I actually paid, however, it worked out that I didn't have to pay it, through this litigation. The east half actually brought $10.00 more than the amount of encumbrance against it, but I forced that issue by bidding on it myself. I bought the surface and the mineral rights

both for $5.50, and sold the surface rights for $3.75. There has been no material change in the surface value of that land between 1924 and 1936.

There was a substantial increase in the value of the mineral rights after my purchase in 1924, and before I sold the mineral rights in 1933, because in 1933 I sold it for $20.00 per acre for the minerals. I did not buy the minerals for $1.70 in 1924, we bought the land and minerals both for the $10,000.00, and perhaps $10,000.00 more contingent upon other matters, but which we did not have to pay, all we actually paid was $10,000.00, after about three years' litigation.

There was a material increase in the value of the mineral rights in this land between 1924 and 1933, but I could not tell you what the increase amounted to on a proportional basis, or on a percentage basis. I sold in 1933 for $20.00 per acre, but the value in 1924 was a speculative value, however, that value was sufficiently definite that I was willing to put my money into it, just as I bought many oil and gas leases on other lands. As to the values of min-
94 erals in the land in 1924, I would think three-fourths of the value of our purchase price was represented by mineral and one-fourth by surface values. If this land was worth $20.00 per acre in 1933 when we sold it, my testimony is not that in 1924 it was worth $15.00 per acre, because we were not paying what we thought we might be able to get out of it, we thought we would make a profit. I could not tell you what was the reasonable market value of the mineral rights in this land in 1924. I think at that time it was proven beyond any question that it would produce gas, and we were hoping it would produce oil and we were buying it just as cheap as we could buy it. I think in 1924 the values of the mineral rights were considerable in excess of what we paid but I couldn't tell you what that value was. I had interests in other land around in that territory, I had a one-fourth interest in fee ownership of the Dial Ranch, twenty miles away, and I had a small interest in two of the gas wells that had been drilled west of the Ozier Ranch. The value of these mineral rights on this particular land would be wholly conjecture. It was a speculative value, the oil business is a speculative proposition. The speculative value was whatever you could get for it.

It is a fact that we paid $5.50 per acre for this land in 1924, and sold the surface rights in 1936 for $3.75. I thought I was buying it for very much less than its value when I bought it, by reason of the peculiar conditions.

I was sufficiently familiar with the fair market value of mineral rights in property located as this property was in the south east section or portion of Moore County, Texas, in 1924, that I was willing to invest my money in and buy it as a speculative proposition. I do not recall any sales of this character of land at that time in Moore County, I lived in Wichita Falls, and I would only be up there occasionally.

95 We had very little income from this property for grazing purposes during the time we held it, during the entire time I would think we received about $1.00 or 75 cents per acre, part of the time we were not able to collect any rent. It was worth about fifteen cents per acre per year, and part of the time we were not able to collect any rents at all. For my one-third interest I received about thirty or thirty-three and a third cents per acre during the entire time I had it, perhaps not much more than enough to pay the advalorem taxes on it. We also sold one pipe line right of way for two or three hundred dollars consideration, and then we sold an oil & gas lease in the property in 1928, for which we got $25.00 per acre, that was a lease on the mineral, to the Amarillo Gas Company—that was in addition to the sale of the entire mineral rights. This was a five year lease and the least was expiring in 1933, and that was the reason we were able to sell the mineral. I did not receive quite one-third of the $25.00, some parties at Graham owned three-eighths interest in the mineral under three sections, but roughly I received one-third, Mr. O'Brien one-third, and Mr. Bivins one-third.

Redirect examination by Mr. WEEKS:

As to the sale under foreclosure that was made in 1924, the lien covered the entire ranch, fee, mineral, and oil, and the east half including the surface and the mineral was the one cut out and sold to satisfy the judgment. That price was paid in cash. The date of the deed for that sale under foreclosure was September 1924. I would say that between that date and the date I made my trade with Mr. O'Brien, which was in January 1924 there had been on change of any significance in the surface value. The trading had gotten considerably more active on minerals, and oil leases, within that time, there was a great deal of interest being manifest in the oil development in that general section during the year 1924.

96 *Stipulation as to income*

Mr. WEEKS. If Your Honor please, the parties stipulate that in their 1933 tax returns, Mr. and Mrs. Perkins reported a net ordinary income, for both of them, of $42,993.74; and an income from capital gain for both of them, of $32,084.84; a total of both ordinary income and capital gain, amounting to $75,078.58.

The east Texas proposition involved in this record came into the ordinary income item, and the Ozier ranch transaction, went into the capital gain item. This was increased by the commissioner of internal revenue upon review, because primarily of the matters here involved, and ordinary net income for both of them fixed at $51,217.01, and the capital gain income at $42,371.21, for both of them, a total of $93,588.22.

Mr. WEEKS. The answer, if Your Honor please, takes care of the allegations as to the amount of taxes paid, date of payment, and thing of that sort.

The answer also contains an allegation that in the event this oil payment item should be excluded from the income of Mr. and Mrs. Perkins, the depletion heretofore allowed them should be correspondingly reduced. The figures are given in the defendant's answers, being a reduction in the depletion allowance of $2,919.16.

The plaintiffs concede the correctness of that allegation under the circumstances which it made, and we say further that with the permission of the Court the parties can readily agree as to the facts and figures to be incorporated into the judgment that might be rendered, and if it is satisfactory with the Court, we will not encumber the record with any detailed calculations of the tax liability and the interest on it.

Whereupon both sides close.

97 *Motion of plaintiff for judgment*

Mr. WEEKS. I have a motion for a judgment for the plaintiff which I would like to file at this time.

The COURT. Is there a motion by the defendant for judgment also?

Motion of defendant for judgment

Mr. POTTER. Yes, sir; the defendant makes a motion for judgment.

III

The plaintiffs then introduced the following additional testimony, to-wit:

JUNE 11, 1936.

J. J. PERKINS, one of the plaintiff, being first duly sworn, examined in chief by Mr. Weeks, testified as follows:

I am J. J. Perkins, one of the plaintiffs in this case, who testified at the previous hearing; in connection with the Ozier Ranch proposition there was some testimony at the previous hearing to the effect that I bought from Mr. Masterson a vendor's lien note on all of the Ozier Ranch, and that at the foreclosure sale a sufficient sum was realized to pay off that note and interest; in connection with that matter I will tell you how that was handled in my tax returns for those years; I bought that note and immediately turned it over to my attorney, and he brought suit to foreclose the lien. Out of the transaction there was a profit of about $2,000.00, brought about largely by reason of the note calling for ten percent attorneys' fees, and the attorney only charged $3,000.00. There was about
98 $2,000.00 in addition to the interest charge on my investment in the note, and that was divided equally between Mr. O'Brien, Mr. Bevans, and myself. That profit was reported for taxation when I received it. It was the interest that I received, and the extra profit, my portion of $11,653.00, were both included in my tax return of that year.

In 1928 myself and associates owned the west half of the Ozier Ranch and made a sale of the oil and gas lease and received a substantial bonus which was reported as income, with a deduction of $5,000.00 as the cost of the lease in my 1928 return. And, when the auditor checked me up, he disallowed any part of the money I deducted for that, the cost of the lease, so that it was then turned in and paid as profit for the year 1928. In other words, the entire portion of this bonus which went to me was treated as taxable income by the taxing authorities, and without any allowance for returning invested capital. However, I think we took depletion on that, but I am not positive—there has been some confusion as to those things. I have some papers here that I can check that from later.

In 1933, after my associates and I had sold the minerals on the Ozier Ranch, we made an effort to dispose of the surface; in that year we made two different efforts to sell it, and offered it for $5,000.00 for my interest in the property, with instructions if they could not get the $5,000.00 that I would take $4,000.00. It was a rough piece of ranch land, and I had no use for it, and the mineral value was the moving incentive when I bought the property; since I sold it, I had no interest in the surface. But I was not able to sell it that year and was not able to sell it until 1936. I believe it is a matter of former evidence, that in my 1933 return I deducted $7,500.00 of my cost as being the cost of the mineral, and that has been disallowed and I have paid taxes on the full amount without deduction of any kind.

99 In connection with my claim for refund I received a letter from the Commissioner of Internal Revenue advising as to the reasons why my claim was rejected. This is the letter here, marked Exhibit A.

Mr. WEEKS. We offer the letter in evidence.

(Sail letter marked "Exhibit A", reading as follows:)

Exhibit A

TREASURY DEPARTMENT,
Washington, Dec. 16, 1935.

Office of Commissioner of Internal Revenue

Address Reply to Commissioner of Internal Revenue and refer to IT:AR:E–1 NF.

Mr. J. J. PERKINS,
Post Office Box 1470, Wichita Falls, Texas.

SIR: Reference is made to your claim for refund in the amount of $1,442.07 income tax and interest for the taxable year 1933.

The basis of your claim is the statement that oil reserves in respect to oil properties in East Texas, as adjusted in the report of the internal revenue agent in charge, Dallas, Texas, are excessive, and

that capital net gain reported from the sale of your interest in all the minerals underlying the Ozier Ranch in Moore County,
100 Texas, was erroneously increased by $7,500.00 in the agent's report.

A review of the case discloses that in accordance with the terms of the contract, whereby a working interest in certain East Texas oil and gas leases was acquired for cash and additional payments to be made out of a fraction of the oil produced, oil payments of $19,229.03 made during 1933 have been included in taxable income subject to percentage depletion and also in leasehold cost returnable through cost depletion. This action is in accordance with the decision of the United States Circuit Court of Appeals for the Eighth Circuit in the case of the Comar Oil Company, 64 Fed. (2d) 965, certiorari denied by the United States Supreme Court, 54 S. Ct. 69, in which it was held that where certain oil and gas leases were transferred to the petitioner by assignments in consideration for a certain amount of money to be paid partly in cash and partly out of oil and gas as produced from the leased property, the royalties paid as deferred payments in 1923 constituted taxable income to the petitioner and also represented capital transactions not deductible as expenses. The treatment of this item in the revenue agent's report is therefore approved by this office.

With reference to the other item covered by your claim, it is disclosed that in 1924 an interest in the Ozier Ranch in fee was acquired at a cost of $10,000.00. In 1933 all of the mineral rights in the property were sold to the Canadian River Gas Company, the share of you and your wife in the proceeds amounting to $31,073.33. In reporting the transaction, three-fourths of the original cost of fee, or $7,500.00, was deducted as being the cost of the minerals sold. The internal revenue agent disallowed the cost claimed in accordance with the decision of the United States Circuit Court of Appeals for the Ninth Circuit in the case of the Coalinga-Mohawk Oil Company, 64 Fed. (2d) 262, certiorari denied by the United
101 States Supreme Court, 54 S. Ct. 69. In that case it was held that where the taxpayer purchased land in 1918 solely as an oil prospect or because of its supposed oil content and in 1921 determined that the land was nonoil bearing and offered it for sale as grazing land, no sale being made until 1923, no deductible loss of a part of the original cost of the property was sustained in 1921 within the meaning of section 234 (a) (4) of the Revenue Act of 1921. Since at the time of the acquisition of the Ozier property by you no segregation of mineral and surface values was made on the basis of $10,000.00 for approximately 1,800 acres of grazing land, it appears that no more was paid for the lands than their value as grazing lands. Therefore the entire amount of $31,073.33 is considered to be taxable income.

For the foregoing reasons, your claim will be disallowed. Official notice of the disallowance of your claim will be issued by registered

mail in accordance with section 1103 (a) of the Revenue Act of 1932.

Respectfully,

CHAS. T. RUSSELL,
Deputy Commissioner.
(Signed) By H. B. ROBINSON,
Head of Division.

The WITNESS. I sold for $6,500.00 in 1936. If I may transgress just a little bit, we bought a third interest in the west half of the Ozier Ranch for $10,000.00, the entire ranch being subject to $60,000.00, vendor lien notes. At the time I made that purchase, I expected the west half to have to pay its proportionate part of these notes, which would have made the west half cost half of that lien, or $30,000.00, plus $30,000.00 we actually paid, would have been $60,000.00 that the west half would have cost us, so that my part would have cost me $20,000.00. That is what I expected to
102 have to pay for it. However, my associate, Mr. O'Brien, said that the assets could be marshaled in such a way that the east half would pay the entire notes and we would not have to pay any thing, and that was worked out through the Courts. And we did not have to pay any part of the vendor lien notes that were a lien on the entire ranch, because the east half sold for a sufficient amount to pay the entire debt, leaving our west half free of any liens.

I did not have any connection with the East half of the Ozier Ranch, except as a lien holder; and had I had to pay my proportionate part of the lien on the west half, the property would have cost me between $11.00 and $12.00 per acre, and I valued at that time, three fourths of the value as mineral and one fourth as surface. At the foreclosure sale that was made in September, after I made this trade in January, 1924, the east half sold for between $13.00 and $14.00, and the increased price over what I thought I had to pay represented the greater interest being manifested in the minerals and oil and gas possibilities in that area from the time I made the purchase until I sold it—or rather, until the east half was sold.

Q. Mr. Perkins, in connection with your work in the oil business, have you had occasion, on numerous times, to observe and ascertain the practices of the Bureau of Internal Revenue, with respect to the taxation of income from gas and oil leases and from gas and oil royalties?

Colloquy

Mr. BACKSTROM: We object to that. In the first place, I think it is immaterial to any issues involved. In the second place, if it is material, it is not the best evidence.

The COURT. I am afraid of that question, Mr. Weeks; I may not see it at all, but I think it is a good objection.

103 Mr. WEEKS. Your Honor, I think the administrative practices of the department of the government, charged with the enforcement of a law, are always material in the interpretation. Sometimes we can have official records showing what those practices are. When we have, I think they are certainly proper evidence.

The COURT. Yes; I think that is correct——

Mr. WEEKS. But I don't think we should be confined to them. In this case, we do not have the detailed official publication as to these practices that I am going to inquire about, that are well known and understood by all who come in contact with the taxation of income from oil and gas. Now, that is a vital factor in this case. In this case the government relies strongly on the Comar Oil Company case, as to the East Texas properties, in which case the Court said it had been the consistent practice of the Bureau of Internal Revenue to make the operator of an oil and gas lease include the proceeds from the sale of all royalty oil as a part of his income. Now I want to prove in several ways that that never has been the practice, from the beginning to this date. Here is a man with experience. I think the evidence in the record is sufficient on that. And the evidence will show he comes in close detailed contact for years with officers of the government who are actually taxing income from oil and gas. We want to prove by him, and from other sources, that the statement of the administrative practice, as contained in the Comar Oil Company case, is a mistake. That it never was the practice. Now, if they have any official regulations to rebut that with, they have their experts down on the next floor, and they are at liberty to try to contradict that testimony.

104 The COURT. It is possible it might be what he himself has suffered, or benefited by, might be admissible. But as a general proposition, an executive officer's attitude toward a law is not very forceful save and except for the basis of future legislation. The Congress sometimes is charged with having taken into consideration the method of enforcement and the construction of a statute. What do you think, Mr. District Attorney, to sustaining your objection, save and except allowing the witness to testify as to what his practice—that is, the practice as to him—might have been?

Mr. BACKSTROM. I think that is immaterial, because the question involved here is a question of income. It is a fundamental question of law. It is not like some of the questions that arise out of the intangible questions or things not definite or certain, like allowance of amount of depreciation, and things of that kind, that are largely a question of practice and procedure, which may vary from year to year. In a case of that kind, I think perhaps the long administrative practice of the treasury department has been construed by the Courts, as perhaps of some value, in construing and in determining a doubtful statute; but where we have a fundamental question, which we have here, what is the income of this plaintiff, or whether it is

income or not, it seems to me that the practice of the department, even if definite, would be immaterial, because this is a fundamental question of law. In a very recent case—I cannot call your Honor's attention to the citation right now—where the Supreme Court made such an observation, where it overruled a long practice of the treasury department for fifteen or twenty years, in which the Supreme Court made such observation that this is a fundamental question, and the practice of the department is not material.

105 And I think, Your Honor, for that reason, it would be objectionable. And I think his particular experience would be of little value anyway, because he is one taxpayer out of a vast number, and even the department dealing with Mr. Perkins might not at all represent the general practice in any way, because we know that the Bureau is a vast organization and naturally in such an organization cases are sometimes settled and disposed of, that are inconsistent, even with the general practice of the Bureau. It is impossible to keep them all in consistent harmony with one another. Unless it is a well defined practice through a great number of years, naturally you will have some cases that are settled that might be out of line. I think for that reason that the actual transactions Mr. Perkins has had with the treasury department would be immaterial, because it would not show any consistent policy. I think the statement of the Court in the Comar Oil case is immaterial. It is a fundamental question as to whose income it is. I cannot say what the practice of the Bureau has been with respect to that, whether or not it has been consistent or inconsistent. As I said in this case, it seems to me it is immaterial. The question of whose income, who owned this oil, and that must be construed and determined upon the basic fundamentals of law and the statute, and the general law as to who is the owner of this property.

Mr. WEEKS. May I just add this: that the very fact that the Courts do frequently refer to these administrative practices shows that those practices are frequently material. The question, as I see it, is whether it is a matter of which the Court would take judicial notice—therefore there would be no necessity of proof—or whether it is a matter to be established by evidence. Now, in certain jurisdictions—for instance, the Board of Tax Appeals—very probably the board

106 would take judicial notice of the practice of the Bureau along that line. Frankly I do not know whether the Court feels that it is sufficiently familiar with the actual practice to take judicial notice of it or not. If we do not take evidence on it, we are liable to be confronted with the proposition, the government saying the practice is one thing and I saying it is another. And we have nothing in the record to show which one is right. So far as the materiality is concerned, I don't think it is a good objection, so far as a trial before the Court like this is concerned. I do believe it is very material to show that the practices are contrary, always have been contrary, to the statement of those practices as announced in the case upon which they are going to rely most strongly.

The COURT. I believe what occurred as to others would manifestly be hearsay. And I think we will allow him to say what experience he has had. I give both sides the exceptions.

The WITNESS. In addition to my own individual income tax matters, I have had connection with income taxes of other concerns with which I was interested, with reference to oil and gas, quite a number of partnerships. Cullum & Perkins; Walker & Perkins; Texhoma Oil & Refining Company, the Faith Oil Corporation, and several others; the Belknap Coal Company, the Belknap Oil Company, and others. This experience has been over a period of twenty years. In these matters it has always fallen to my lot personally to handle them with the Bureau of Internal Revenue at Dallas and at Washington—it has always fallen to my lot to handle income tax matters of these companies and partnerships with which I have been associated; some more so than others, but in the main they have all come under
107 my direct supervision, and I have always talked with the revenue agent and gone over the report and the analysis and conferred on all matters. I have been down here a number of times, and in the early days I made a number of trips to Washington, staying there several days at a time and discussing the matter with the income tax authorities for myself and for partnerships. Some of those interests with which I have been connected have been royalty interests and some lease interests. There has not been a year in the last eight or ten years that I have not had as much as eight or ten or fifteen or twenty thousand dollars' royalty interest in addition to what my income may have been from leasehold interests.

Q. Now, Mr. Perkins, in your particular cases, your individual cases, and those that you come in direct contact with, in the manner that you have related; what has been the practice of the Bureau of Internal Revenue, as to whether or not they required a lessee to report as a part of his income, the oil or proceeds of the oil, which went to the lessor as royalty?

Mr. BACKSTROM. We object to that, on the grounds heretofore stated. I think the testimony ought to be confined to specific dealings, rather than practice. I do not think Mr. Perkins' experience has been such as to qualify him to speak as to the general practice. And I think the testimony ought to be confined, if it is going to be admitted, to specific rulings upon specific cases.

The COURT. Well, it is limited to such cases as have come under his personal supervision and control as an executive, or interested person, in these concerns. I overrule the objection.

Mr. BACKSTROM. We except.

108 The WITNESS. We have never reported the royalty from the leasehold interest which we are operating on any lease we have operated, we have never been asked to include the royalty oil and receipts therefrom; and we have never included it because it was, as I understood the practice, and as they were told to me, that was revenue to be reported on by the owner of the royalty and not the lease operator. On the royalty interest I own, I re-

ported it as my income, because I understood it to be the practice of the department that that was required of me, and I reported it and paid for it in every instance. That applies to myself and every company I have been associated with. That has never been changed by the examining officer, on any income tax return I have made for myself or my associates at any time; it has been consistent from 1916, for the last twenty years, down to the present time. They customarily come in and examine very carefully, and usually have a government engineer to check over all of that part of the reports having to do with oil and gas properties, whether it is royalty or whether it is working interest.

Q. What has been your personal experience and observation in those cases like this; if you have had personal experience and observation; take an oil and gas lease which provides, as to the gas, that the lessee is to pay the lessor a fixed sum per well per annum for each well from which gas is sold off of the premises; what has been the practice, in those cases to which we are referring, of the Bureau of Internal Revenue, in regard to that rental or payment per well per annum to the lessor?

A. We have paid the cash rentals, provided in the leases, as a gas royalty, and have charged it up as an expense item and it has been allowed in every instance by the Internal Revenue Department.

Q. In those cases, is it the practice for the lessee to report one hundred percent proceeds from the sale of the gas, where he paid a cash rental——

109 A. Yes, sir, we would report all of the revenues we received from the properties, upon which we would be entitled to depletion.

Q. And deduct the cash rental?

A. As an expense item.

Q. Mr. Perkins, reverting to those Brawley and Branson and Hammond properties in East Texas; did you or not ever sell, or attempt to sell, that portion of the oil applicable to those oil payments to Branson and Hammond and Brawley?

Mr. Backstrom. We object to that. It is immaterial; it encumbers the record, and does not help us in this case at all.

The Court. I do not see the materiality of it.

Mr. Weeks. In the previous trial there was some question made as to the fact that this portion of the oil was his, and that he claimed it. I just wanted to go into that to show that he never attemped to sell it and did not claim it as his own, but always recognized the ownership in Branson and Hammond and Brawley, to that portion of the oil applicable to the oil payment.

The Court. Well, it is a question of law. I do not see any special objection to the question, if you want him to answer it.

A. I have not, because I had nothing whatever to do with it.

The Witness. Would it be permissible for me to state how the Internal Revenue Agent who handled the Branson and Hammond oil payment, in working up cost depletion, handled that

110

matter? I will state that in the calculation of our cost depletion allowance, in respect to this Branson and Hammond property, that the Revenue Agents and the engineers did not treat this $395,000.00 oil payment as a part of the cost of our property, like they treated the cash and notes. In arriving at cost for a given year, they would add to the cash cost of the property only the amount of the oil payment produced in the previous year; so if there had been $30,000.00 produced in 1932 for the oil payment, and the cash cost of the property was $155,000.00, that plus $30,000.00, which would be the basis they would use for establishing cost depletion for the next year and from that they would take the depletion taken in prior years; in other words, they did treat the cash we paid and the notes we paid, as part of our cost, for the purpose of determining cost depletion; but they did not treat any part of the oil payment except that part as had been retired in a previous year; except such part as had been retired in a previous year.

Cross-examination by Mr. BACKSTRON:

Q. ——

A. My income tax returns are reported on the cash receipts and disbursement basis.

J. L. MCMAHON, a witness for the plaintiff, being first duly sworn, examined in chief by Mr. Weeks, testified as follows:

My name is J. L. McMahon. I live in Wichita Falls, and work most of the time in Forth Worth. I am connected with the Texas Company, as Division Manager of the producing—department; my territory is the northern part of Oklahoma, north Texas, west
111 Texas, west central Texas, Arizona, and New Mexico; that includes what we commonly refer to as the Panhandle of Texas, and Moore County. I have been connected with the Texas Company on two occasions, about twenty-one or twenty-two years altogether. The Panhandle territory has been under my supervision since its inception, the first development and prior thereto. My primary duties is the supervision and acquisition of oil properties, purchasing leases, etc. By reason of that connection, it has become necessary for me to acquaint myself with the situation with respect to oil possibilities in this west Texas territory and particularly Moore County, with the values that were being paid from time to time for oil and gas leases and for minerals.

I know the location in Moore County of the properties known as the Ozier Ranch, and the west half thereof, approximately fifty-three hundred acres. I have been acquainted with that territory since the first gas well came in north of Amarillo, which was probably in 1919. At that time that territory was under my supervision for the Texas Company. The west half of the Ozier Ranch territory was valuable, as to the minerals, in January 1924. In my opinion, the fair and reasonable market value of the minerals under the west half of the Ozier Ranch in January 1924, excluding from that

any valuation of the surface, was anywhere from $12.50 to $25.00; that territory looked very attractive about that time from a mineral lease standpoint.

Cross-examination by Mr. POTTER:

I do not know when Mr. Perkins acquired that property. I do not know that Mr. Perkins paid $5.50 per acre for that property; that is, for the mineral and surface rights. If he did pay that price for it, I would still say that the market value was probably
112 $12.50 or $25.00 per acre, because I do not know under what condition Mr. Perkins purchased it, and I would say if he got it at $5.50 that was a very low price.

Offer in evidence

Mr. WEEKS. We offer in evidence certain portions of the deposition of C. H. CLARK, reading as follows:

My name is C. H. Clark. I live in Wichita Falls, and have lived there forty six years. I have been in the oil business since 1912 and am now in that business. I have been trading in oil properties and producing oil and gas. During that period I have operated in Electra, in southern Oklahoma, and later in the Breckenridge country and in the Plains country, west Texas. I have operated what is called the Panhandle section. I was manager of the Red River Oil Company at Electra first, had an interest with them in the property—and also had charge of their property in southern Oklahoma at Healdton; then was president of the Shamrock Oil Company for a good many years, operating in Oklahoma, north of Wichita Falls, and in the Breckenridge country; then later in the Amarillo section, in Hutchinson, Gray, and Wheeler Counties.

My trading in the oil business began in 1912 in the Electra territory, and I bought most of the property that the McMahon Oil Company acquired in that section back in the old days. Then after that I was trading and dealing in oil properties for the McMahon Oil Company until they sold out their properties. Then later on operated as President of the Shamrock Oil Company; then we had a little organization known as the Shamrock Petroleum Company; three of us owned that. The Red River Oil Company was organized at Electra before the McMahon Oil Company came into existence. That was always a separate corporation, and still is; they are practically the same people; they still own that property.
113 I have operated in Moore County, Texas, and in Hutchinson County, and in that section of the Panhandle. I think we went up there about 1919 or 1920; I am not sure about the date right now, because I have not had occasion to look that up—I would say 1919; at least it was several years before 1924, on up through 1924, 1925, and 1926, I operated there at the Shamrock Oil Company and we bought leases and drilled some gas wells, and had quite a little property over that country. We did not produce much oil in that country, however. We traded in leases.

Because of my experience and my work in the Texas Panhandle, and my position, I think I have a general idea of the values of minerals or mineral rights in lands in Moore County during 1924 and 1925. I know the property known as the Ozier Ranch in Moore County; I was over that property shortly after I went up there, I don't know what date, but about 1920. I was over that property and frequently crossed that ranch, going to the well we were drilling. I have a general idea of the value of the property in that territory known as the Ozier Ranch, in January 1924, as to the value of the minerals. Previous to 1924, we leased a block of land from Carry Thompson, which I would say is four or five miles west of the Ozier Ranch. I have a map that will show exactly, but that is approximately correct. Also at the same time we had some leases down southwest of the Ozier Ranch; they came up within two or three miles, probably, I could not say about the distance, because I haven't checked that on the map. I have a map here which shows the Ozier Ranch, and some of this Thompson land is further over here and we had acreage in here; this place here is known as the Masterson Well; the Masterson Oil Company was organized, in which the Shamrock had a half interest, in these properties. The Masterson well was west of the Ozier Ranch about six miles.

114 That well was drilled in 1920. It produced nine million feet of gas. We also drilled a well in section 42, in the Sneed land, which is northwest from the Ozier Ranch about three miles. That well was drilled in 1922, and was a good gas well. I think that was the first well on the Sneed ranch. I believe the first well on the Sneed ranch was drilled in 1921. * * *

I have stated that in my opinion this property, the minerals in this property, had a market value in January, 1924; it is hard to place that in my mind right now, but I will state just now that at that time I would place those mineral rights at $15.00 or $20.00 per acre, in a block of stuff like that, that you could control.

Offer in evidence

Mr. BACKSTROM. We wish to offer the balance of the deposition in evidence, the entire testimony:

I had general charge of those drilling operations, and the acquisition of those leases on those wells which we drilled; I made the trade for the property. We organized the Masterson Oil Company, and as I remember now, it is a little hazy in my mind, that the Shamrock had a half interest in those properties. They organized and put this company at Amarillo, Mr. R. G. Masterson was president.

I had been on the Ozier Ranch, as I remember, Mr. Wells, a friend of mine in Amarillo, and a man in the real estate business, Bill O'Brien, went with me, I think, out on the Ozier Ranch, at one time, to look it over. We were looking the ranch over because it was offered for sale. That must have been around 1922, or some-

where about there. They carried me out there and asked me to check it over and look it over and see it with that in view. I would say that the Ozier Ranch did have prospect and values as to minerals in 1924, because gas was then becoming quite valu-
115 able in that country. There had been wells drilled west of this ranch, and as I remember now, there had been a well drilled east of this ranch, back in that direction. Some gas over here, and it was considered gas territory at that time when I was on it. I went there and looked it over with the idea that we might buy it, and I thought probably that we would, but this Shamrock Oil Company was owned largely by Waxahachie people, Mr. Homer Chapman, said we had better not spend too much money in that country, and I dropped the matter.

I would say that Mr. Perkins bought this ranch in 1924; I will say two years previous to that time, when I was three, that is just an off-hand guess as to the time. * * *

I do not think there was any material difference in the value of the east and west half, for mineral purposes, of the Ozier Ranch in January 1924. This Ozier Ranch was about as rough as there is in all of the country as I remember it. You see, the Canadian River cuts along the south side of the Ozier Ranch and it goes up next to the prairie, then these gulches come in. It is very rough. It is just as rough as you can find in that country. I was looking at it for the mineral rights. I was not caring anything about the surface rights at the time I looked at it. It is purely a ranch proposition, as far as the surface is concerned.

The subsequent course of developments up there established the fact that the Ozier Ranch was productive of gas—it was all productive of gas—so considered in that whole territory. You could get gas wells any place you might drill. Some hard spots you don't get near as much as you do at others, it is indefinite, about the size of the well. I don't know when the first well was drilled upon that land—I don't remember. With reference to this map, as the Ozier Ranch, it showed some drilling having been done on that, and that was done, it was considered proven territory. For instance, there
116 was a well drilled over southeast of that ranch by Jim Whittington at an early date, and that well produced considerable oil, and they developed some good oil in that territory I mentioned; southeast, across the river from the Ozier Ranch. There is a large gas field in the Panhandle of Texas, in Moore County. I think the Panhandle field is classed as about the largest field in the world—that is, this Panhandle gas field. It is about one hundred and sixty miles long, extends from Sayre, Oklahoma, and runs to Dumas in Moore County. I would say it is from ten to thirty miles wide, something over a million acres in it, and about twenty trillion feet of gas, supposed to be. This Ozier ranch is in what is known as the sweet gas area, that is, in the sweet gas area. In this country you get what we call sour gas. I am talking about the territory northwest of the Ozier Ranch, with reference to the sour gas. The sour

gas has greater sulphur content in it, and it is not as good for domestic purposes, where it is used with an open stove. There may be some other chemicals in it, but that is one thing about it, it is not really safe to use in an open stove.

Cross-examination by Mr. BACKSTROM:

I do not remember that I bought any mineral leases, with reference to oil and gas, along about 1924, in the vicinity of the Ozier Ranch. I don't remember that we bought any acreage about that time. You see, this stuff, we got back in 1919 and 1920, some of that was based upon drilling purposes. We took one lease up here that cost us over one hundred thousand dollars, and put down a well on it. Of course, instead of buying the lease we were doing some developing. Here is a general map of the country northeast of the Ozier Ranch. We bought some acreage in there along about 1923 or 1924. It is
117 about five miles northeast. I cannot tell you from this map, but about four or five miles northeast, there is one tract we had there definitely, we thought, I think that was in 1924. We just bought a lease on that land. We did not buy the mineral rights. We were organizing the Shamrock Petroleum Company and we bought that land from Major Reed, a man who had a good deal of property in that country. We paid him $65,000.00 in cash and $65,000.00 in stock in the Shamrock Petroleum Company and we guaranteed that his stock would at least net him par. He would not sell the land outright, and we made him that guarantee, that was about five miles northeast of the Ozier Ranch. That was practically $100.00 per acre for that property. When the Sneed well was being drilled, and we started that well, we sold some of the acreage around that well, and that was in 1922 that this well was finished. We were trying to hedge on it a little bit, if I remember, we sold that stuff from $10.00 to $20.00 per acre. We were getting gas, and we were drilling the Sneed well for both oil and gas, we contemplated at that time building a line into Amarillo and putting the gas in Amarillo. This Sneed well was drilled in 1922. We did not get any oil, but we did get gas. Shortly after that, we sold that property, and I presume that gas is being used from that well at this time in Amarillo, we sold our interest in that property to the Prairie Oil & Gas Company. That was in 1926. I do not know what we got per acre for the mineral rights on that land. I will tell you, there would be a record of it, this Masterson Oil Company, in which some Amarillo people owned an interest, in fact, I went up there and suggested that we put this thing, a separate company from the Shamrock, and we would take our interest in it, half interest, I think that was the way it was. They sold out, though, for considerable money, to the Prairie Oil & Gas Company. What they got, I do not know, but we
118 dropped out of the picture. The Shamrock sold its interest to the Prairie Oil & Gas Company, and the Prairie Oil & Gas Company then bought this interest of the Shamrock, which gave them the whole property. They bought these holdings. I do not

know what we received for the mineral rights on that land; it was included in the general sale. We sold this piece over here. We paid $100.00 per acre for, we sold in 1926 when we sold the property around the Ozier Ranch for mineral purposes. I do not know what the valuation of the property was. We had about eight thousand acres of this land running through here, oil on some of it and gas on some of it, I am sure it was worth a great deal more to the Prairie Oil & Gas than it was to us, from the fact that they built a line to Denver, and have been drawing gas from this territory. That was their object in buying up this property, I think.

After we drilled this well, on the Sneed land, we drilled a well on northwest of this on the Gober land. That was two or three years after this well was drilled down here—after the Sneed well was drilled. That was a gas well, we did not find any oil. I don't remember how much gas it produced, it was what we called a good well, probably twenty or thirty million feet. There was not much sale at that time out there for gas at the well, because there was no way to get it out. The gas, in 1924, had a potential value to the folks that needed it. There was the Prairie Oil & Gas Company getting ready for the line to Denver. Potentially it had a great big value. When you talk about gas land worth $10.00 or $15.00 per acre, that is like getting it for nothing. In fact, this well up here cost, I would say, this well on the Gober cost about $100,000.00 to drill it. They drilled three holes before they got through with it.

It had not been definitely determined in January, 1924, that the Ozier Ranch was not oil land. I cannot refer to those dates exactly, but a well across here, east of that, known as the
119 Whittington well showed considerable oil, I would say that well was six or eight miles east, it was across the Canadian River. Of course, it was presumed—nobody knows—but it was presumed at that time that there was deep oil in the vicinity of the Ozier Ranch. It had a potential value as oil property. I will say this, illustrating our idea about it, because we bought some stuff in here and some other property closer to this Ozier Ranch, but I cannot tell you just where it was, but it was closer in than this McDonald tract, about five or six miles from the Ozier Ranch. I think we bought it in 1924. The only piece I remember, as to the price, definitely, is this 1,280 acres here from Major Reed; also a piece from Will Herring, that we paid about $100.00 per acre for. We paid $100.00, that is, $50.00 cash and a note, half cash and half in a note. Now, if I were at home, I could give you the records and tell you the exact date, but that is approximately correct. This other piece closer up, we paid something like the same price, I would say $100.00 per acre. I would not testify as to the price definitely, because I don't remember, but I remember about this other, because that is definite, my mind is clear. It was impressed upon my mind that Major Reed said he would not lease the land, that he would not sell it, and I went to him with that proposition.

I said, "If you will come in with us on this piece of land, if you will come in and join us on this deal, we will give you half cash and stock for the balance in the Shamrock Petroleum Company." We gave him a positive guarantee that he would get his money back out of the stock. He was a very peculiar fellow to trade with, and a very fine gentleman.

In January, 1924, I looked over the Ozier Ranch with the idea in mind that I might buy this property, but our folks decided that they did not want to put any more money in that territory. I do not know whether we would have paid $15.00 per acre for the
120 mineral rights on the Ozier Ranch or not. I did not recommend to my company the purchase of this Ozier Ranch, we had plenty of acreage up there, and had spent a good deal of money and were spending a good deal more, and we were buying some high priced stuff. I do not know what I could have bought the mineral rights on the Ozier Ranch for at the time I was negotiating for it. After I was on this land it sold very promptly, after I was out on this land. I do know that there was a sale consummated in a very short time. I do not know how they figured the minerals at that time. There was another feature about it, I remember this about it, that it was tied up, there was a mortgage against it, they were swapping horses, trying to save their hide at that time—the detail I do not remember. I cannot place any similarly situated land as the Ozier Ranch in that vicinity where the mineral rights sold for as much as $15.00 or $20.00 around January 1934. There was trading going on all the time. Most of that stuff was worked on that kind of basis. I will show the point, how those values came in; if you got four sections of land, somebody would give you that four sections of land, because they wanted a $25,000.00 or $30,000.00 or $40,000.00 well drilled, and it was very expensive, which made our property cost quite a little money.

I do not know how much gas this Masterson well produced, I think it might have been nine million feet. That seems to be about seven or eight miles from the Ozier Ranch. Nine million feet of gas would be a commercial well. There was no sale for gas out in that territory at that time, because the lines had not come in. We do not buy gas on that basis, if we have a good gas well out there, I can go up there today and show you a gas well that is not selling gas, but it is worth a good deal of money. For instance, we sold a gas well over here about this time, we sold it
for $40,000.00, just as a gas well, and it was producing thirty
121 or forty million feet of gas. We sold it about 1924 or 1925. The Empire built the line in there; I don't know when their line came into that field.

As to why I valued this land at $10.00 or $15.00 per acre, the question comes up in my mind, and you asked me why they did not have a price of more than that, and it is because if you consider now a man gets gas in that territory and you see it now, and you go back and talk about it, and at that price it was picking it up for nothing.

I think the mineral rights on the Ozier Ranch in 1924 could have been sold for as much as $15.00 or $20.00 per acre. If I had been looking for mineral land in that territory, my remembrance is that that would have been a very reasonable, fair price. The conditions since that time has justified that would be getting it for nothing. Because gas land in that territory now is worth—I might state to you gentlemen this—in talking about the value of a gas well, up in this sour gas territory there is not much difference in the value of it now; they figure that a section of land up there might be worth $250,000.00, that is, the gas that is under it. When I state the value as $15.00 or $20.00 of this land in 1924, my memory runs back to that time; if I say that that was a fair price for it, and then if conditions after that time did not justify that statement, then you would say I was really mistaken about my remembrance of the situation back there.

I would consider a value on land as fair that had any prospect and the possibility of giving a man a good return on his investment. I would say the mineral value of that land today would be $50.00 or $75.00 or $100.00 per acre. I will say this, that I contemplated paying for a piece of gas land up there recently $400.00 per acre, and it had oil possibilities and gas possibilities. That is a lease. I am talking about the lease. We did make this kind of a trade recently, one hundred and sixty acres of land on which a well had been drilled,
making about thirty-five million feet of gas, and there is an
122 overriding royalty on that piece of land, and no cash paid for
the lease. The over-riding royalty is one-sixteenth for wells of one hundred barrels or less, and if it gets up about one hundred barrels there is an over-riding one-eighth on it. That is up in this territory, there is some oil being developed around in that territory. It has oil possibilities. The people do not know anything about the value of that gas up there; if they did they would not be wasting a billion feet every day. It is a crying shame to sit around here and let that energy go to waste. There is a proration market up there on that gas. Most of the wells have a market for the gas. They are trying to enforce this proration law. Of course, they have not had much success with it so far, but the major companies now realize that they must prorate that gas out there, and take it out of that field, or they will have serious trouble.

GEORGE H. ABBOTT, a witness for the plaintiff, being first duly sworn, examined in chief by Mr. Weeks, testified as follows:

My name is George H. Abbott. I live in Tulsa, Oklahoma. I am a public accountant, and have been practicing that profession since 1921. I am a certified public accountant in Oklahoma and Arkansas. I am connected with the firm of Barrow, Wade & Guthrie. I supervise all income tax work, federal and state. I have a card that permits me to practice before the Bureau of Internal Revenue, and have been practicing before them since 1921. The major part of my work has to do with the taxation of income from oil and gas. During this

period my work has been in Oklahoma and Texas, from 1921 to date; also in Arkansas.

I am familiar with the practices of the Bureau of Internal
123 Revenue with respect to the taxation of income from oil and gas, and particularly as to royalty owners and lessees; and with the practices which they follow, in determining the income, gross and net income, from those sources. In addition to that, I have had occasion to observe their actual handling of those matters in specific cases.

Q. What has been the nature of your personal experience in those matters; in other words, what has been your opportunities to observe personally their practices in handling those matters?

Mr. BACKSTROM. We object to that as immaterial. It is not the best evidence. The best evidence of the Bureau's practice is its own acts. What it does in cases that are matters of public record, if the plaintiff desires to put that in evidence before the Court, I think Your Honor, that should be presented to the Court, rather than the testimony of some witness as to what has been done.

The COURT. Well, it is the same question I ruled upon a moment ago. I want to be sure that he speaks only of the matters he knows, by actually seeing, and not what somebody told him.

Mr. WEEKS. Mr. Abbott, base all of your answers, entirely upon matters which have come within your direct personal observation and knowledge, matters you have handled and have seen.

Mr. BACKSTROM. We except.

The WITNESS. I either prepare myself or supervise the preparation of federal income tax returns and in the preparation of those
124 returns, we had to be guided, as to our opinion, as to the requirement of the law and the regulations; following the examination by revenue agents, with whom I may have had frequent conferences. We also have conferences with the Internal Revenue Agent in Charge, or conferences with his representatives. We also have conferences in Washington, and in some cases we file appeals to the Board of Tax Appeals, and have tried cases there in which I have been co-counsel, or counsel of record. I have done all of those things myself. I handle from twelve to twenty cases each year.

Mr. POTTER. We object to this line of testimony.

Q. Tell us this, Mr. Abbott, as you have observed actually by experience and practice in this work, what has been the practice of the Bureau of Internal Revenue in those cases which you observed as to whether or not they required the lessee under an oil and gas lease to report as a part of his income, the oil and gas which went to the lessor or royalty owner, or the money which went from the sale of that oil or gas to the lessor or royalty owner.

The COURT. Now, before he answers that, they wish an exception.

Mr. BACKSTROM. We renew our objection to this specific question.

The COURT. Let the exception be noted.

The WITNESS. As far as my observation and knowledge goes, the commissioner has never required the lessee to include in his taxable income the royalty received by the lessor.

I have never had occasion to observe the practice in case of gas wells where there was a flat rental per year for the production of gas from the wells. I have had occasion to observe, on several occasions, the practice with respect to oil payments.

Q. What has been the practice of the Bureau of Internal Revenue, as you have observed it, in those cases in which an oil and gas lease was transferred—let us say for a cash consideration—but the assignor reserves a certain fraction of the oil until that oil produced so much money, let us say one-fourth of seven-eighths, until the assignor got $100,000.00; where there was an express reservation in the assignment, what has been the practice of the bureau in those cases, that you observed, as to whether or not that one-fourth of seven-eighths was treated as the income of the assignor or the assignee?

Mr. BACKSTROM. We object to that.

The COURT. Overrule the objection.

Mr. BACKSTROM. We except.

The WITNESS. I don't know that I ever recall having a case in which the assignment made a specific reservation, that is where the term "reserved" or "reservation" was used. I don't think I have not had occasion to deal with a lease where it said "except one-fourth" until any specific amount has been paid.

Q. Do you know what the practice is, from your general experience, in handling tax matters, as to the way they treat such a situation?

Mr. BACKSTROM. We object to that.

The COURT. Sustain the objection.

Mr. BACKSTROM. We except.

The COURT. I want to ask you a question. You answer so far as you know. What do you mean by that reservation?

The WITNESS. In what question was that, Judge Atwell?

Mr. WEEKS. It was the question as to what the Commissioner's practices were?

The WITNESS. Well, I was just trying to stay within the ruling of the Court, that I am limited here to what I, myself, have seen.

The COURT. That is what you mean?

The WITNESS. Yes, sir.

I do not know of any case, in my experience, where they held otherwise.

J. J. PERKINS, recalled, examined in chief by Mr. Weeks, testified as follows:

When I was on the stand awhile ago, there was perhaps some confusion as to the question of whether or not I had been allowed depletion in my 1928 return in respect to the bonus on this oil and gas lease. Since I left the stand, I have checked into that, and I find that we were not allowed any depletion. We were allowed neither depletion nor any part of the cost for 1928, the entire cash bonus was reported, and the revenue agents checked up, as income.

Plaintiffs Rest.

Statement by Mr. Backstrom

Mr. BACKSTROM. In the answer which was filed to the amended petition the defendant has made an alternative allegation that one fourth of the cost of producing the oil from these leases should be disallowed as operating expense in the event that the Court holds that one fourth of the income, the income in question here, should be eliminated from the plaintiffs' taxable income. So we take the position that if that income is not included that one fourth of the cost of producing it, which has been allowed as a deduction, would be disallowed. In the return, as the record shows, they were allowed, as cost of producing the oil, $17,384.00, and we have claimed one fourth of that should be disallowed, which would be $4,346.21. I would like, in order to show what was allowed as a cost of producing this oil as the expense, we introduce in evidence the revenue agent's report, which set up the additional tax, which is being sued to be recovered, and with specific reference to Schedules 1, 1a, item 18 and C, and Schedule 3, and exhibits D, D1, and D-2.

Colloquy

Mr. WEEKS. We have no objection to the introduction of the data to which he has referred, but I think his offer should be limited to that, because the report contains a lot of figures.

The COURT. Well, you cannot make an agreement with him?

Mr. BACKSTROM. If Mr. Weeks will agree that the plaintiff was allowed as a deduction, in taking out all the oil from these
128 leases which were involved in this question, the sum of $17,-384.85, and that we allowed that amount as a part of Mr. Perkins' operating expense for the year in determining the net taxable income, I think that would take care of all we wish to prove by this offer.

The COURT. I think you are entitled to one or the other under your pleadings.

Mr. WEEKS. We think this Exhibit D shows all of the data necessary.

Mr. BACKSTROM. It does not show the computation. There might be some question about it being carried forward.

Mr. WEEKS. I will say that I am willing to agree. We agree that in determining these plaintiffs' net income they were allowed to deduct the amount of the cost of operating the east Texas leases actually paid in that year. These costs cover not only the cost of the production of the share of the oil which went to them, but the share of the oil which went to the royalty owners and to the holders of the oil payments—. This Exhibit D-2 correctly reflects the calculation made by the commissioner and carried into his final calculation of

tax liability, showing the amount of expenses which he allowed to Mr. and Mrs. Perkins and to their co-operator, Green.

Mr. BACKSTROM. We will accept that statement. Also the exhibit D–2 be introduced rather than Exhibit D–1.

Mr. WEEKS. That is satisfactory.

(Said instrument marked "Plaintiff's Exhibit B" and reading as follows:)

129 *Exhibit B*

In re: J. J. Perkins et ux. Exhibit D–2

Perkins and Green—East Texas Properties

Allowable Depletion

	Barrett & Wencker lease	Fenton lease	Fuller lease	Brawley lease	Total
All sales per return	$18,589.10	$13,510.67	$13,860.65	$3,063.41	$49,023.83
Payments out of oil	7,354.31	5,360.09	5,500.98	1,013.65	19,229.03
	25,943.41	18,870.76	19,361.33	4,077.06	68,252.56
Deductions—					
Operating expense including overhead, taxes, and insurance	8,998.67	7,307.33	8,974.44	2,204.42	27,484.86
Depreciation	2,611.20	1,835.73	1,976.22	861.69	7,284.84
Total deductions	11,609.87	9,143.06	10,950.66	3,066.11	34,769.70
Net before depletion	14,333.54	9,727.70	8,410.67	1,010.95	33,482.86
50% of net	7,166.77	4,863.85	4,205.34	505.47	16,741.43
27½% of oil sales	7,134.44	5,189.46	5,324.36	1,121.19	18,769.45
Cost depletion	2,503.49	3,544.59	4,170.43	6,222.33	16,440.74
Allowable depletion	7,134.44	4,863.85	4,205.34	6,222.33	22,425.96
Depletion claimed	4,286.10	9,465.33	8,648.56	6,108.31	28,508.29
Increase (decrease)	2,848.34	(4,601.48)	(4,443.21)	114.02	(6,082.33)

A. H. FREEMAN,
Internal Revenue.

Approved August 31, 1935.

(Signed) ALEXANDER D. BELL,
Engineer Revenue Agent.

Approved:

L. P. ANDERSON,
Chief, Natural Resources,
Section: _____

131 J. J. PERKINS, recalled, examined in chief by Mr. Backstrom, testified as follows:

I am reasonably familiar with the operations of these leases which are shown in Exhibit D–2. I do not think I could explain what items are covered by operating expenses, which were allowed with respect to those leases for the year 1933; it is a matter of record on my books. I could check it up if I had an opportunity to do so, but that is a matter of detail handled through the office. As to the

operations covered by those expenses, you have here an item of operating expense, including the overhead, taxes, and insurance. That would include the lease men, and minor repairs, and it would include ad valorem taxes, compensation insurance, superintendents salary, allocated to those properties, and I think it would include the office expense; however, that was only $50.00 per month, as I recall it. I know that we paid a large amount of interest on money that we owed in connection with the operation and development of these properties, and I think that the interest was included in this, not necessarily an expense item, but it was money we owed in connection with the properties, one way or the other. I imagine it was included in that item. The items included in the expense here would represent more than the cost of taking the oil out of the ground, it would represent the interest items, which was not part of the expense of producing the oil. Leaving out the interest item, I would say the expense items all represent the cost of taking the entire oil from these leases, that is in the main, with reference to the details, I could not say exactly, but that is approximately correct. This is evidently the amount that the revenue agent allowed as being the amount. The presumption is that that would represent the cost of taking the oil out of those leases, and that would also include the item of interest. I would assume that this item of $27,000.00
132 includes all of the cost of taking out the oil and interest items, and those are the only items I would know it included, because I have no detailed check on it.

Colloquy

Mr. BACKSTROM. I renew my offer of the Revenue Agent's report as to the schedules 1, 1a, item 18 and C, and Schedule 3, and Exhibit D, D1, D2.

Your Honor, the schedule, as I see it, that is in evidence, does not exactly show just exactly what I think we ought to show was allowed, and for that reason, in view of the testimony of Mr. Perkins, I would offer this for the purpose of showing what we allowed.

The COURT. I thought we had passed that. You wanted to show that $17,384.85 had been allowed by the government in this particular transaction?

Mr. BACKSTROM. Yes.

The COURT. And $4,000 and some odd dollars was this taxpayer's part of it?

Mr. BACKSTROM. Yes.

The COURT. I asked Mr. Weeks if he would agree to it, and I understood him to say that he agreed to what he did say in the record, and to schedule D-2. Doesn't that furnish what you want?

Mr. BACKSTROM. I don't think it does.

133 The COURT. Is there any objection to these figures that he has in mind?

Mr. Weeks. The figures are all right. We have no objection to the Revenue Agent's report going in, because I am sure Mr. Backstrom will agree to eliminate any immaterial portions. The purpose was to keep from encumbering the record.

The Court. Have you any objection to these figures?

Mr. Weeks. This exhibit shows overhead, operating expense, including overhead, taxes, insurance, $27,484.86, depreciation on physical equipment of $7,284.84, total of $34,769.70. That is for the Perkins and Green interest together; in other words, it is the operating expense, overhead, taxes, and insurance for 1933, plus depreciation. The government's position is that if we exclude from income one fourth of seven eighths of the oil then we should exclude one-fourth of the operating expenses. We are willing to agree that these figures were allowed us in computing our taxable income.

The Court. But you do not have the figures that he wants.

Mr. Backstrom. One-half of that went to Perkins.

The Court. You have figured thirty-four thousand dollars, plus, now he does not say thirty-four thousand dollars plus, he says seventeen thousand three hundred eighty four ($17,384.85) dollars, eighty-five cents, then one fourth of that.

134 Mr. Weeks. Yes.

The Court. That is what he wants you to say, that this is correct, if you will agree to that.

Mr. Weeks. Yes; I think that is all right. I will develop it by cross examination.

The Court. I do not like to transgress this secret process that the taxpayer has the benefit of, unless we have to do it. I am not sure that a Court could do it in a civil proceeding. Of course, I am sure it could be done in a criminal proceeding. That is the only reason I see here.

Mr. Weeks. I did not think of that, but certainly the Revenue Agent's Report is a detailed reflection of all of a man's financial affairs that no one has any particular business with.

The Witness. The oil from the leases shown on Exhibit 2, was taken out by myself and my associates. The oil represented the one-fourth involved in this controversy here, was taken out and the cost of that was included in the total cost shown on Exhibit D-2.

Examination by Mr. Weeks:

The item on the schedule D-2, Defendant's Exhibit B, $7,284.84, goes to make up the total of $34,769.70, half of which is applicable to me, that represented the depreciation on the physical equip-

135 ment to be placed on the lease, the derrick, casing, tanks, tubing and other things. That belonged to me and my associates. When I say myself and associates, I mean the Faith Oil Company, and Mr. Green. These expenses, operating expenses, include overhead, taxes, and insurance actually paid by myself and Mr. Green and the Faith Oil Corporation. We are not going to get anything back from Bronson or Hammond or anybody else, there is no way

by which I am going to recoup any of these expenses I have paid out.

Defendant rests.

Mr. WEEKS. The defendant has raised some question about the refund claim on a small portion of this. We want to offer in evidence the refund claim filed by Mr. Perkins, with the understanding that it is stipulated that the other refund claim filed by Mrs. Perkins is identical.

Mr. BACKSTROM. It is agreed to.

(Said instrument introduced, marked "Exhibit C" and reading as follows:)

Exhibit 6

JAN. 10, 1936.

IT:C:CC-4-CCP.

In re: Claim for refund of $1,442.07 for the year 1933

Mr. J. J. PERKINS,
Postoffice Box 1470,
Wichita Falls, Texas.

SIR: Reference is made to Bureau letter dated December 16,
136 1935, wherein you were informed that the claim for refund indicated above would be disallowed. The letter also stated the reasons for the proposed disallowance.

The claim having been disallowed or rejected on Schedule numbered 22535, this notice of disallowance is sent to you by registered mail as required by Section 1103 (a) of the Revenue Act of 1932.

Respectfully,

GUY T. HELVERING,
Commissioner,
(Signed) By CHAS. T. RUSSEL,
Deputy Commissioner.

ib
IT:AR:E-1.

NF (Stamped) Received Dec. 18, 1935, Claims Control Section. Dec. 16, 1935.

"Omitted because identical with Plaintiffs' Exhibit A, as per stipulation of counsel copied at page one hereof.

* * * * * * *

Exhibit

Statement attached to the Claims for Refund of Income Taxes paid for the Calendar Year 1933 by J. J. Perkins and Wife, Mrs. J. J. (Lois) Perkins, Wichita Falls, Texas, P. O. Box 1470.

Under date of October 15, 1935, there was transmitted to the above named claimants the report of Internal Revenue Agent A. H. Freemon, with respect to the tax liability of the above named for

the calendar year 1933. This report is dated September 17, 1935. This report is hereby referred to and made a part hereof for all purposes.

The additional taxes shown by said report were paid to the
137 Collector of Internal Revenue at Dallas, Texas, on October 24, 1935. The payments made were as follows:

J. J. Perkins—additional income:	
Tax	$1,315.37
Interest thereon	125.70
Total	$1,442.07
Mrs. J. J. Perkins—additional:	
Income tax	$1,316.37
Accrued interest	125.70
Total	$1,442.07

The taxpayers had theretofore paid for the calendar year 1933, in regular quarterly installments in 1934, the following sums as income taxes for the year 1933:

J. J. Perkins	$3,070.14
Mrs. J. J. Perkins	$3,102.14

The taxpayers seek the refund of all of the taxes paid on October 24, 1935, with the interest paid thereon, or such greater or lesser amounts as may be refundable because of the facts hereinafter set forth.

Among other changes made in said Revenue Agent's report were adjustments on oil reserves in respect to oil properties in East Texas in which these taxpayers have an interest.

The taxpayers do not agree to this adjustment. They believe it is incorrect and that the reserves as adjusted are materially excessive. Because, however, of the application of percentage depletion to these properties, it appears from the taxpayers' calculations that this adjustment does not increase their tax liability for the year 1933.

If, however, it should develop upon consideration of this claim
138 for refund, or any subsequent proceeding based thereon, that the determination of cost depletion is necessary to arrive at their taxable income, then the taxpayers say that said reserves as adjusted in said Revenue Agent's report are materially excessive.

In the year 1933 these taxpayers owned a 3/8ths interest in such leasehold rights to oil and gas leases in Texas as were granted by an assignment and conveyance executed on July 24, 1931, by Mamie S. Hammonds, O. O. Hammonds, and Fred P. Branson to Faith Oil Corporation. A copy of this conveyance is attached hereto and made a part hereof, but there is omitted from said copy the detailed description of the various tracts of land covered by said assignments as such descriptions are not material to a consideration of the questions here presented. Another 3/8ths of such interest was owned by W. J. Green and 1/4th was owned by the Faith Oil Corporation.

Said assignment provided for what is commonly referred to as the "oil payment" in the sum of $395,000.00; said instrument providing,

in substance, that a certain percentage of the oil produced from the properties covered by said conveyance was to go to the assignors above mentioned until they had received from this source oil of the value of $395,000.00. Said payment being entirely contingent upon the production of enough oil from said property so that the specified percentage would produce for said assignors the sum above mentioned.

In the year 1933 the above named assignors received oil of the value of $19,229.03 by virtue of so much of the oil payment as was applicable to the percentage of interest in said property owned by these taxpayers and W. J. Green.

The examining officer has included said sum as income derived by Perkins and Green from their joint operations. (See Exhibit D, page 14 of said Revenue Agent's report.) This increases the alleged gross income of the taxpayers from these operations by one
139 half of said sum. Taxpayers say that this sum is not their income, but that the oil from which this income was derived and the proceeds from the sale of said oil were in truth and in practical effect, as well as in law, the income and property of the said assignors, and that this sum should be excluded from the computation of their income.

Claimants admit that by said report depletion was allowed with respect to said sum and that, if their position is maintained, it will be necessary to recalculate depletion on that account.

In the year 1933 the taxpayers sold their interest in all of the minerals underlying the Ozier Ranch in Moore County, Texas. They reported a capital gain from this source of $23,573.33 (See 5th Item, Schedule 4, page 7 of said Revenue Agent's report). This was increased by the Revenue Agent by the sum of $7,500.00, and to this increase taxpayers protest and claim a refund of so much of the tax paid as was based thereon.

The taxpayers acquired an undivided 1/3rd interest in this ranch in 1924 at a cost of $10,000.00. The ranch contained 5,400 acres. At the time this ranch was acquired by the taxpayers and associates, the mineral content thereof was its principal element of value. The taxpayers would not have considered purchasing said land but for this mineral value. In their opinion, then and now, at least 3/4ths of the cost and value when purchased was attributable to this mineral value. Because of this, they say that when, in 1933, they sold and conveyed all of their interest in these minerals they were entitled to deduct, in arriving at their taxable income therefrom, so much of the cost thereof as was attributable to the mineral value; that this was at least $7,500.00, and that the Revenue Agent erred in disregarding this cost in determining their taxable income. In the alternative, the taxpayers say that they are entitled to depletion upon all of the consideration received for the minerals sold.

140 "Omitted because identical with Plaintiffs' Exhibit 1", as per stipulation of counsel copied at page one hereof.

* * * * * * *

Exhibit

CLAIM

To be filed with the collector where assessment was made or tax paid

The collector will indicate in the block below the kind of claim filed, and fill in the certificate on the reverse side.

(Collector's Stamp.) (Dated received ----------)

(x) Refund of tax illegally collected.

( ) Refund of amount paid for stamps unused, or used in error or excess.

( ) Abatement of tax assessed (not applicable to estate or income taxes).

(Stamped): Received Dec. 9, 1935. Claims Control Section.

STATE OF TEXAS,
County of Wichita, ss:

Name of Taxpayer or purchaser of stamps (type or print), J. J. Perkins. Business address, Box 1470, Wichita Falls, Texas. Residence, 3301 Harrison Blvd., Wichita Falls, Texas.

The deponent, being duly sworn according to law, deposes and says that this statement is made on behalf of the taxpayer named, and that the facts given below are true and complete:

1. District in which return (if any) was filed, Dallas, Texas.

141 2. Period (if for income tax, make separate form for each taxable year) from 12-31, 1932, to 12-31, 1933.

3. Character of assessment of tax, Income taxes.

4. Amount of assessment, $--------; dates of payment—See statement attached.

5. Date stamps were purchased from the government----------

6. Amount to be refunded including interest paid, or such greater or lesser amount as may be legally refundable, $1,442.07.

7. Amount to be abated (not applicable to income or estate taxes $----------).

8. The time within which this claim may be legally filed expires, under Section 322 of the Revenue Act of 1932, after October 24, 1937.

The deponent verily believes that this claim should be allowed for the following reasons:

See Statement attached.

(Stamped) Bureau of Internal Revenue Mail Room. 1935. Dec. 9 AM. 947.

(Signed) J. J. PERKINS.

Sworn to and subscribed before me this 7th day of November 1935.

[SEAL] S. A. MAN, *Notary Public.*

(See instructions on Reverse Side.)

Certificate

I hereby certify that an examination of the records of this office shows the following facts as to the assessment and payment of the tax:

142

Character of assessment and period covered	List	Year	Month	Account page	No. or line	Amount assessed	Paid; abated; or credited		Pd. Ab. Cr.
							Date	Amount	
1933	IT	1934		214856		$3,070.14	4-14-34	$746.25	Pd.
						3.78	6-14-34	792.60	"
				Into Acct. 9-B			3-15-34	25.00	"
							9-14-34	755.04	"
							12-15-34	755.03	"
1933 Add'l	193-IT	1935	Oct.	510082		1,316.37	10-25-35	1,442.07	"
						125.70			
					Total	4,515.99	Total	4,515.99	

I certify that the records of this office show the following facts as to the purchase of stamps:

To whom sold or issued	Kind	Number	Denomination	Date of sale or issue	Amount	If special tax stamp, state:	
						Serial No.	Period commencing

Rejected 22535. I. T. Schedule

Claim examined by NF Amount claimed, $1,442.07.
Claim approved by ---------- Amount allowed, $---------
Chief of Division. Amount rejected, $1,442.07.

(Signed) W. A. THOMAS,
Texas 2nd,
Collector of Internal Revenue Dist. B. B.

Committee on Claims

143

Instructions

1. The claim must set forth in detail and under oath each ground upon which it is made, and facts sufficient to apprise the Commissioner of the exact basis thereof.

2. Claim should be sworn to by the taxpayer, if possible. Whenever it is necessary to have the claim executed by an attorney or

agent, on behalf of the taxpayer, an authenticated copy of the document specifically authorizing such agent or attorney to sign the claim on behalf of the taxpayer shall accompany the claim. The oath will be administered without charge by any collector, deputy collector, or internal revenue agent.

3. If a return is filed by an individual and a refund claim is thereafter filed by a legal representative of the deceased, certified copies of the letters testamentary, letter of administration, or other similar evidence must be annexed to claim, to show the authority of the executor, administrator, or other fiduciary by whom the claim is filed. If an executor, administrator, guardian, trustee, receiver, or other fiduciary files a return and thereafter refund claim is filed by the same fiduciary, documentary evidence to establish the legal authority of the fiduciary need not accompany the claim, provided a statement is made on the claim showing that the return was filed by the fiduciary and that the latter is still acting.

4. Where the taxpayer is a corporation, the claim shall be signed with the corporate name, followed by the signature and title of the officer having authority to sign for the corporation.

144

IV

Thereupon the testimony was concluded and both parties closed, and each party presented to the Court a Motion for judgment in favor of such party and, after argument, the Court granted the Plaintiffs' Motion for Judgment in part and denied the same in part, and granted Defendant's Motion for Judgment in part and denied the same in part.

V

Wherefore, the Plaintiffs pray that this, their Bill of Exceptions, may be allowed, settled, and signed.

HARRY C. WEEKS,
Attorney for Plaintiffs,
J. J. Perkins and Mrs. Lois Perkins.
Staley Building, Wichita Falls, Texas.

It is agreed by and between the counsel for the respective parties that the above and foregoing is a full, true, and correct statement of the proceedings had upon the hearing of the above numbered and entitled cause, and of the evidence adduced thereat, and that the same shall constitute the Bill of Exceptions on appeal with reference to such matters as herein stated.

HARRY C. WEEKS,
Attorney for Plaintiffs.
CLYDE O. EASTUS,
FRANK B. POTTER,
J. L. BACKSTROM,
Attorneys for Defendant.

Order approving bill of exceptions

The above and foregoing, having been agreed to by counsel for the respective parties hereto, is hereby approved and ordered
145 filed as a part of the record in this cause as the Bill of Exceptions, which shows a full, true, and correct statement of the proceedings had upon the trial of the above styled and numbered cause, and a full, true, and correct statement of the evidence adduced thereat.

Dated this the 7th day of July, A. D. 1936.

WM. H. ATWELL,
United States District Judge.

In United States District Court

Petition for appeal and order allowing same

Filed July 6, 1936

To the Honorable Wm. H. Atwell, Judge of said Court:

The above named plaintiffs, J. J. Perkins and wife, Mrs. Lois Perkins, feeling themselves aggrieved by judgment made and entered in this cause on the 11th day of June, 1936, do hereby appeal from the said judgment to the United States Circuit Court of Appeals for the Fifth Circuit for the reasons set forth in the Assignment of errors which is filed herewith.

Wherefore, premises considered, your Petitioners pray that their appeal be allowed; that citation issue as provided by law, and that a transcript of the record, proceedings and papers upon which said judgment was based, duly authenticated, be sent to the United States Circuit Court of Appeals for the Fifth Circuit sitting at New Orleans for the correction of the errors complained of and herewith assigned, and that the proper order touching the security to be required of them to perfect their appeal be made.

(Signed) HARRY C. WEEKS,
WEEKS & MORROW,
Attorneys for Plaintiffs.

146 *Order*

The foregoing petition for appeal is this day granted and the appeal allowed, conditioned upon the Plaintiffs giving bond for costs, as required by law, in the sum of Five Hundred ($500.00) Dollars.

Dated the 6th day of July, 1936.

(Signed) WM. H. ATWELL,
United States District Judge.

In United States District Court

Assignment of errors

Filed July 6, 1936

Now come the Plaintiffs and file this their Assignment of Errors as a basis for their appeal from the judgment herein rendered against them (in so far as it relates to the matters covered by the following Assignment of Errors) on the 11th day of June, 1936, and say that the same is erroneous and unjust to the Plaintiffs, in this:

I

The Court erred in denying Plaintiffs' motion for judgment, in so far as the same related to the inclusion in the Plaintiffs' taxable incomes, for the year 1933, of any portion of the oil (or the proceeds from the sole thereof) produced from the oil and gas leases described in the assignment from Branson and Hammonds to Faith Oil Corporation, which went to Branson and Hammonds under the rights and titles retained by them (Branson and Hammonds) in said assignment to have delivered to them one-fourth (¼th)
147 of the oil produced and saved therefrom until they had received $395,000.00, or oil of that value; and in failing to award Plaintiffs a recovery of so much of the income taxes and interest paid by them for the year 1933, as was based upon the inclusion of any of the aforesaid amount as a part of their taxable income for the year 1933.

II

The Court erred in holding that so much of the income taxes and interest collected by defendant from Plaintiffs for the year 1933, as was based upon including, as a part of the Plaintiffs' taxable incomes for 1933, the proceeds from the sale of so much of the oil produced in 1933 from the properties described in the assignment to Faith Oil Corporation from Branson and Hammonds as went to said Branson and Hammonds under the rights and titles retained by said Branson and Hammonds in said assignment to have delivered to them one-fourth (¼th) of the oil produced and saved from said properties until they, the said Bransom and Hammonds had received $395,000, was properly assessed and collected, and in failing and refusing to allow Plaintiffs a recovery of such taxes and interest.

III

Since the undisputed evidence in this case showed the following facts:

(1) That Branson and Hammonds retained, in the assignment which they made to Faith Oil Corporation, the right to have deliv-

ered to them one-fourth (¼) of all of the oil produced from the properties described in said assignment until they had received $395,000.00;

148 (2) That the Plaintiffs acquired as their community property, prior to 1933, and held throughout 1933, three-eighths (⅜ths) undivided interest in such rights, titles, and estates to the properties there described as were originally assigned by Branson and Hammonds to Faith Oil Corporation, and held same subject to the aforesaid right of Branson and Hammonds;

(3) That oil was produced from said properties in 1933 and one-fourth (¼th) thereof delivered to the pipe lines serving said properties to the credit of Branson and Hammonds, and that said one-fourth (¼th) was sold by Branson and Hammonds to various oil purchasing concerns who paid Branson and Hammonds directly for the same, and that no part of the proceeds from the sale of said one-fourth (¼th) of the said oil produced in 1933 was ever received by Plaintiffs;

(4) That the total amount received by Branson and Hammonds from the sale of said one-fourth (¼th) of the oil produced in 1933, was $24,287.10, and that there was included in the final determination and assessment of the Plaintiffs' income tax liabilities for 1933, three-eighths (⅜ths) of said sum, to wit, $9,107.69, and that a portion of the income taxes, and interest, collected by defendant from Plaintiffs, on October 25, 1935, was attributable to the inclusion of said sum as a part of the plaintiffs' taxable incomes;

(5) That Plaintiffs had duly filed claims for the refunding of said taxes and interest; that said claims had been rejected, and that Plaintiffs were authorized to maintain this suit for the recovery of such taxes and interest;

The Court erred in denying Plaintiffs a recovery of such taxes and interest, and in holding that said sum of $9,107.69 was properly included as a part of their taxable income for the year 1933.

149 IV

The Court erred in denying Plaintiffs' motion for judgment, in so far as the same related to the inclusion in the Plaintiffs' taxable incomes, for the year 1933, any portion of the oil (or the proceeds from the sale thereof) produced from the property described in the oil and gas lease from E. H. Brawley and wife, Cora Brawley, to W. J. Green, which went to E. H. Brawley under the rights and titles retained by him in said oil and gas lease to have delivered to him one-fourth (¼th) of seven-eighths (7/8ths) of the oil produced and saved therefrom until he had received Forty-Five Thousand ($45,000.00) Dollars, or oil of that value, and in failing to award Plaintiffs a recovery of so much of the income taxes and interest paid by them, for the year 1933, as was based upon the inclusion of any of the aforesaid amount as a part of their taxable incomes for the year 1933.

V

The Court erred in holding that so much of the income taxes and interest collected by defendant from Plaintiffs, for the year 1933, as was based upon including as a part of the Plaintiffs' taxable income, for 1933, the proceeds from the sale of so much of the oil produced in 1933 from the property described in the oil and gas lease from E. H. Brawley and wife to W. J. Green, as went to said E. H. Brawley under the rights and titles retained by him in said oil and gas lease to have delivered to him one-fourth (¼th) of the oil produced and saved from said property until he, the said Brawley, had received Forty-Five Thousand ($45,000) Dollars, was properly assessed and collected, and in failing and refusing to allow Plaintiffs a recovery of such taxes and interest.

150 VI

Since the undisputed evidence in this case showed the following facts:

(1) That E. H. Brawley retained, in the oil and gas lease which he and his wife made to W. J. Green, the right to have delivered to him one-fourth (¼th) of seven-eighths (7/8ths) of all of the oil produced from the property described in said oil and gas lease until he had received Forty-Five Thousand ($45,000.00) Dollars;

(2) That the Plaintiffs acquired as their community property, prior to 1933 and held throughout 1933, three-eights (3/8ths) undivided interest in such rights, titles, and estates to the properties there described as were originally leased by E. H. Brawley and wife to W. J. Green and held same subject to the aforesaid right of E. H. Brawley;

(3) That oil was produced from said property in 1933 and one-fourth (1/4th) of seven-eighths (7/8ths) thereof delivered to the pipe lines serving said property to the credit of E. H. Brawley, and that said one-fourth (1/4th) of seven-eighths (7/8ths) was sold by E. H. Brawley to various oil purchasing concerns, who paid him directly for the same, and that no part of the proceeds of the sale of said one-fourth (¼th) of seven-eighths (7/8ths) of the said oil produced in 1933 was ever received by Plaintiffs;

(4) That the total amount received by E. H. Brawley from the sale of one-fourth (¼th) of seven-eighths (7/8ths) of the oil produced therefrom, in 1933, was $1,351.53, and that there was included, in the final determination and assessment of the Plaintiffs' income tax liabilities for the year 1933, three-eighths (3/8ths) of said sum, to-wit, $506.83, and that a portion of the income
151 taxes and interest collected by defendant from Plaintiffs on October 25, 1935, was attributable to the inclusion of said sum as a part of the Plaintiffs' taxable incomes;

(5) That Plaintiffs had duly filed claims for the refunding of said taxes and interest; that said claims had been rejected, and that

Plaintiffs were authorized to maintain this suit for the recovery of such taxes and interest;

The Court erred in denying Plaintiffs a recovery of such taxes and interest and in holding that said sum of $506.83 was properly included as a part of their taxable incomes for the year 1933.

VII

The Court erred in limiting Plaintiffs' recovery of costs to such costs as were incurred with respect to the issue as to which Plaintiffs prevailed, and in not allowing Plaintiffs to recover from defendant all costs in this behalf incurred.

Wherefore, Plaintiffs pray that the judgment be reversed and that the United States Circuit Court of Appeals for the Fifth Circuit grant such relief as the nature of the case demands.

(Signed) HARRY C. WEEKS,
WEEKS & MORROW,
Attorneys for Plaintiffs, J. J. Perkins and Mrs. Lois Perkins.

[Bond on appeal for $500.00 approved and filed July 6, 1936, omitted in printing.]

153 [Citation in usual form showing service on Clyde O. Eastus et al., filed July 7, 1936, omitted in printing.]

154 In United States District Court

Praecipe for transcript of record

Filed July 7, 1936

To the Clerk of the District Court of the United States for the Northern District of Texas, Dallas, Texas:

SIR: You will please include in the transcript of the record for the appeal in the above entitled cause the following papers, proceedings, and documents:

1. Plaintiffs' First Amended Original Petition.
2. Defendant's First Amended Original Answer.

155 3. Plaintiffs' Motion for Judgment filed June 11, 1936.
4. Defendant's Motion for Judgment filed June 11, 1936.
5. Judgment of the Court.
6. The Opinion of the Court Delivered June 11, 1936.
6-a. Application for Extension of Time and Order Thereon.
7. Plaintiffs' Bill of Exceptions.
8. Application for Appeal and Order Allowing same.
9. Assignment of Errors.
10. Appeal Bond and its Approval.
11. Citation on Appeal and Acknowledgment of Service Thereof.
12. This Praecipe and Proof of Service Thereof.

(Signed) HARRY C. WEEKS,
WEEKS AND MORROW.
Attorney for J. J. Perkins and Mrs. Lois Perkins.

156 It is agreed between counsel for the respective parties in the above cause that the foregoing papers, proceedings, and documents constitute a complete record on appeal in said cause.

Executed this 7 day of July 1936.

(Signed) HARRY C. WEEKS,
Attorney for J. J. Perkins and Mrs. Lois Perkins.
(Signed) CLYDE O. EASTUS,
(Signed) FRANK B. POTTER,
(Signed) J. L. BACKSTROM,
Attorneys for W. A. Thomas, Collector of Internal Revenue for the Second District of Texas.

157 [Clerk's Certificate to foregoing transcript omitted in printing.]

158–160 [Omitted.]

161 [Caption omitted.]

162 In United States District Court

Defendant's application for extension of time

Filed June 26, 1936

Comes now the defendant by Clyde O. Eastus, United States Attorney, and Frank B. Potter, Assistant United States Attorney, and moves the Court that the present term of this Court be continued as to this cause for a period of 75 days so that the defendant may prepare and have settled such statement of evidence, bill of exceptions, and other matters as the defendant may deem necessary and proper.

(S.) CLYDE O. EASTUS,
United States Attorney.
(S.) FRANK B. POTTER,
Assistant United States Attorney.

163 In United States District Court

Order extending time

Filed June 26, 1936

On this the 26 day of June, A. D. 1936, came on to be heard the motion of the defendant that the present term of the Court be continued as to this cause for a period of 75 days; and the same having been considered by the Court, it is hereby ordered and decreed that the present term of this Court be, and the same is hereby, continued and extended as to this cause for 75 days from and after this date, so that the defendant may prepare and have settled such statement of evidence, bill of exceptions, and other matters as the defendant may deem necessary and proper.

(S.) WM. H. ATWELL,
United States District Judge.

In the United States District Court

Petition for appeal

Filed Sept. 9, 1936

To the Honorable William H. Atwell, Judge of Said Court:

W. A. Thomas, Collector of Internal Revenue, defendant in the above entitled and numbered cause, feeling himself aggrieved by the judgment made and entered herein on the 11th day of June
164 1936, does hereby appeal from said judgment to the United States Circuit Court of Appeals for the Fifth Circuit for the reason set forth in the Assignment of Errors which is filed herewith.

Wherefore, premises considered, your petitioner prays that his appeal be allowed; that citation issue as provided by law; and that the transcript of the record, proceedings and papers upon which said judgment was based, which have heretofore been sent to the United States Circuit Court of Appeals for the Fifth Circuit sitting at New Orleans, in the appeal of the plaintiffs heretofore taken, be supplemented so as to include defendant's petition for appeal and assignment of errors, the court's order allowing same, and such other papers deemed necessary for defendant's appeal.

Your petitioner further prays that the proper order relating to the security for this appeal be entered.

CLYDE O. EASTUS,
United States Attorney,
FRANK B. POTTER,
Assistant United States Attorney,
J. L. BACKSTROM,
Attorney, Treasury Department,
Attorneys for Defendant.

165 In United States District Court

Order allowing appeal

Filed Sept. 9, 1936

On the 9th day of September, A. D. 1936, came on to be heard the petition of the defendant for an appeal herein, and it appearing to the Court that said petition has been presented in due season, it is hereby ordered that an appeal from the judgment entered in this cause to the United States Circuit Court of Appeals for the Fifth Circuit be, and the same is, hereby allowed, and that the certified transcript of pleadings, stipulations and proceedings herein which have heretofore been transmitted to the United States Circuit Court of Appeals for the Fifth Circuit at New Orleans in the appeal of the plaintiffs herein, be supplemented by the petition for appeal of the defendant, the assignment of errors, the order allowing same, and such other instruments and papers deemed necessary by defendant.

This appeal being prosecuted by defendant, a collector of internal revenue, on instructions of the Attorney General of the United States of America, no bond on appeal shall be required.

WM. H. ATWELL,
United States District Judge.

166 In United States District Court

Assignment of errors

Filed Sept. 9, 1936

To the Honorable William H. Atwell, Judge of Said Court:

Now comes the defendant and files this, his Assignment of Errors, as the basis for his appeal from the judgment herein rendered against him (in so far as it relates to the matter covered by the following Assignment of Errors) on the 11th day of June 1936, and says that the same is erroneous and unjust to the defendant in this:

I.

The Court erred in denying that part of the defendant's motion for judgment relating to the Ozier Ranch property, and sustaining plaintiffs' motion for judgment therefor, and finding that plaintiffs were entitled to deduction of $7,500.00 which represented three-fourths of the original purchase price of said Ozier Ranch property.

Wherefore, defendant prays that the portion of the judgment relating to the deduction allowed plaintiffs in the matter of Ozier Ranch property be reversed and that the United States Circuit Court
167 of Appeals for the Fifth Circuit grant such relief as the nature of the case demands.

CLYDE O. EASTUS,
United States Attorney,
FRANK B. POTTER,
Assistant United States Attorney,
J. L. BACKSTROM,
Attorney, Treasury Department,
Attorneys for Defendant.

In United States District Court

Waiver of issuance and service of citation on appeal

Filed Sept. 12, 1936

Now comes the plaintiffs, J. J. Perkins; and wife, Lois Perkins; by their attorneys of record, Weeks and Morrow, and Harry C. Weeks, and having been furnished copy of defendant's petition for appeal and assignment of errors herein, waive the issuance and service of citation, or further notice on appeal in this cause.

WEEKS & MORROW,
HARRY C. WEEKS,
Attorneys for Plaintiffs.

168 In United States District Court

Praecipe for record

Filed Sept. 9, 1936

To the Clerk of the District Court of the United States for the Northern District of Texas, Dallas, Texas:

SIR: You will please include in the supplemental transcript of the record for the appeal in the above entitled cause the following papers, proceedings, and documents:

1. Defendant's Application for Extension of Time and Order Thereon.
2. Petition for Appeal.
3. Order Allowing Appeal.
4. Assignment of Errors.
5. Waiver of Issuance and Service of Citation on Appeal.
6. This Praecipe and Proof of Service Thereof.

CLYDE O. EASTUS,
United States Attorney,
FRANK B. POTTER,
Assistant United States Attorney,
J. L. BACKSTROM,
Attorney, Treasury Department,
Attorneys for Defendant.

169 [Clerk's Certificate to foregoing transcript omitted in printing.]

170 That thereafter the following proceedings were had in said cause in the United States Circuit Court of Appeals for the Fifth Circuit, viz:

Argument and submission

Extract From the Minutes of November 11, 1936

No. 8172

J. J. PERKINS, ET AL.

vs.

W. A. THOMAS, COLLECTOR OF INTERNAL REVENUE

On this day this cause was called, and, after argument by Harry C. Weeks, Esq., for appellants, and Milford S. Zimmerman, Esq., Special Assistant to the Attorney General, for appellee, was submitted to the Court.

172 *Argument and submission*

Extract From the Minutes of November 11, 1936

No. 8219

W. A. THOMAS, COLLECTOR OF INTERNAL REVENUE

vs.

J. J. PERKINS, ET AL.

On this day this cause was called, and, after argument by Milford S. Zimmerman, Esq., Special Assistant to the Attorney General, for cross-appellant, and Harry C. Weeks, Esq., for cross-appellees, was submitted to the Court.

174 *Opinion of the court filed December 18, 1936*

In the United States Circuit Court of Appeals for the Fifth Circuit

Nos. 8172 and 8219

J. J. PERKINS, ET AL., APPELLANTS AND CROSS-APPELLEES

vs.

W. A. THOMAS, COLLECTOR OF INTERNAL REVENUE, APPELLEE AND CROSS-APPELLANT

Appeal and Cross-Appeal From the District Court of the United States for the Northern District of Texas

(December 18, 1936)

Before FOSTER and SIBLEY, Circuit Judges, and STRUM, District Judge

SIBLEY, Circuit Judge: Additional income taxes for the year 1933 were assessed against and paid by J. J. Perkins and his wife
175 Lois Perkins. Denied refund, they sued the Collector of Internal Revenue in the District Court, waiving jury trial. There was no conflict in the evidence. During 1931 they acquired along with others a transfer of an oil and gas lease on Texas land made in consideration of a small amount of cash and of $395,000 to be paid out of oil produced and saved. During the tax year 1933, oil having been discovered, large sums were paid to the transferors of the lease on account of this "oil payment." The Commissioner considered these sums to be income of the transferees subject to tax, though immediately paid over to the transferors, and assessed additional taxes accordingly. The district judge upheld him, preferring the reasoning in our case of Pugh vs. Commissioner, 49 Fed. (2) 76, and Comar Oil Co. vs. Blount, 64 Fed. (2) 965, from the

Eighth Circuit, to our later case of Commissioner vs. Fleming, 82 Fed. (2) 325. On another item the Perkins were shown to have purchased an interest in a tract of Texas land in 1924 for $10,000, largely because of its supposed mineral content, and had in 1928 made an oil and gas lease on it, getting a bonus therefor of about $45,000, and in the tax year 1933 they sold all their remaining interest in the minerals in the land for about $36,000. The land was completely disposed of in 1936 for about $7,000 more. In their tax return for 1928 the taxpayers claimed but were disallowed any return of capital by depletion or otherwise in taxing the bonus money. In 1933 the Commissioner again refused any deduction from the receipts from the sale of the minerals. The district judge upon uncontroverted evidence that when the land was purchased three-fourths of its value was fairly attributable to its minerals allowed deduction of $7,500 as cost of the interests sold. The Collector appeals on account of this latter ruling, and the taxpayers on account of the former.

We will examine first the cost deduction. The taxpayers
176 invested $10,000 in the purchased land including its minerals. They must be allowed a recovery of their investment, since gain only can be constitutionally taxed as income. Eisner vs. McComber, 252 U. S. 189. The statutes provide for the deduction of cost from purchase money in simple sales, and for depletion deductions where exhaustible elements of the land are drawn upon in realizing income from it otherwise than by a sale. Though in Texas an oil lease is a conveyance of an interest in land, for income tax purposes the lease is treated not as a sale but a means of getting income from the land, and not only the royalty as rent but the bonus or lump consideration also is income from the land. Burnet vs. Harmel, 287 U. S. 103. The recovery of capital to be lost in the contemplated withdrawal of the oil and paid for in advance by the bonus is taken care of by the depletion allowance to be deducted therefrom. Palmer vs. Bender, 287 U. S. 551. The taxpayers here were entitled to a depletion allowance when they made their lease for a bonus in 1928 whether they got it or not; and on a subsequent sale the statute requires that in making a deduction for cost previous deductions for depletion shall be taken into consideration. Rev. Act 1932, § 113 (b) (1). "Proper adjustment in respect of the property shall in all cases be made * * * (B) in respect of any period since Feby. 28, 1913, for exhaustion, wear and tear, obsolescence, amortization, and depletion, to the extent allowed (but not less than the amount allowable) under this Act or prior income tax laws. Where for any taxable year prior to the taxable year 1932 the depletion allowance was based on discovery value or a percentage of income, then the adjustment for depletion for such year shall be based on the depletion which would have been allowable for such year if computed without reference to discovery value or a percentage of income." The sentence last quoted applies to the bonus received in 1928 for the oil lease. At that time the depletion allowance,

177 if one had been made, would have been based on discovery value, or would have included that value in the percentage rate fixed by Congress, so that in making the adjustment on the sale in 1933 the whole allowance in 1928 would not be deducted from the cost but only a less amount reflecting a depletion based on original cost. The Collector is wrong in contending that the whole cost of the property is offset by the percentage depletion allowance that could have been made in 1928. He is wrong both because such percentage depletion is forbidden to be used in the adjustment as just pointed out, with the result that a depletion short of exhaustion can never properly exceed the whole cost; and wrong because a depletion allowance in 1928 was expressly refused. We have not a case where the taxpayer neglected to claim his deduction at the time it was due him and thus lost it. It was claimed and disallowed, and as Palmer vs. Bender, supra, had not then been decided, the ruling was acquiesced in as correct. It is manifestly unjust to allow the Government, having thus informed the taxpayer he could not have the deduction for his invested capital in 1928, now to say he could have it only then. Nor does the statute require any such attitude, for as above quoted it requires only that "proper adjustment" shall be made. Under the circumstances here disclosed nothing should be deducted from the cost basis because of this depletion allowance for 1928 which was claimed but was rejected.

The minerals were sold out in 1933 but not the surface rights. The District Judge apportioned the cost between the estate sold and that retained. This was found practicable and is fair. No regulation has been cited to us to the contrary. The minerals in the ground may be sold separately from the surface rights just as part of the acreage may be separately sold. When part of the whole is sold off an apportionment of the cost is usual if it can be made.

178 When the part retained is of little value compared to what is sold not to allow a deduction for the cost of what is sold might result in a most unfair taxation. The action of the district judge was correct.

On the question touching the oil payment we must disapprove the judgment. In dealing with income taxes in connection with transactions in oil leases this court at first attempted to apply the peculiar law of Texas or Louisiana and the resulting technical relationships of the parties. Such decisions were made in Pugh vs. Commissioner, 49 Fed: (2) 76; Harmel vs. Commissioner, 56 Fed. (2) 153; and Palmer vs. Bender, 57 Fed. (2) 33. The two last were taken to the Supreme Court and reversed, 287 U. S. 103, 287 U. S. 551, that court declaring that the income tax laws ought to have a uniform operation in all States and that income and deductions ought to result in like situations everywhere; and that a broad view ought to be taken of the transactions, deductions for depletion, for instance, being allowable to all who had an "economic interest" in the reserve in the ground regardless of the technical title to it. Adopting that

view this court in Commissioner vs. Fleming, 82 Fed. (2) 324, did not follow its decision in the Pugh case, but said: "We have thus looked at the transaction broadly as was done in Palmer vs. Bender (287 U. S. 551) and not technically as was done in the Pugh case." While the reasoning of the Pugh case may be correct upon a question of title to the oil and the ordinary consequences of title, we cannot regard it as a valid authority on the present question. Since the decision of Palmer vs. Bender other circuits have reached the conclusion we came to in the Fleming case touching the socalled "oil payments." Commissioner vs. Elliott Petroleum Co., 82 Fed. (2) 193; Alexander vs. Continental Petroleum Co., 63 Fed. (2) 927.

The instrument transferring the lease here involved uses this language: "Now, therefore, in consideration of the sum of
179 $10 * * * and the further sum of $395,000 to be paid out of the oil produced and saved from the hereinafter described lands, and to be one-fourth of all the oil produced and saved from the premises until the full sum of $395,000 is paid, we * * * do hereby bargain, sell, transfer and assign, and convey all our rights, title, and interest in and to said leases * * *. As hereinbefore stated $395,000 is to be paid to (transferors) out of the oil produced and saved from the leased premises, which payments shall be made by the pipe line Company or other purchaser of said oil and shall be one-fourth of all the oil produced and saved until the full sum of $395,000 is fully paid * * * which oil payments shall be made direct to (transferors) by the purchaser as the oil is run. The said $395,000 is payable out of oil only if, as, and when produced * * * and shall not be a personal obligation of the assignee." Whosesoever may be the technical title to the oil in the ground or that produced and saved until sold, it is plain that the transferors have an economic interest in both, and a right to specific performance of the agreement to sell and pay over a fourth of the proceeds of oil produced. According to the Fleming case they are entitled to a depletion allowance on what they get, and that means that what they receive is income and not purchase money. The share of the proceeds of the produced oil retained by the transferees is, of course, their income on which they too are entitled to an allowance for the depletion caused to them. But the portion of the proceeds going to the transferors is not the income of the transferees. It is not the proceeds of the transferees' oil paid over to the transferors in discharge of an obligation, as the district judge because of the broad words of conveyance held. Looking to the whole instrument, and noting especially that the proceeds of one-fourth of the oil saved is never to be paid by the buyer to the transferee-producer, but is to be paid direct to the transferor, and
180 that the transferee owes no money debt, but only the duty to sell the oil and submit to a division of the proceeds by the purchaser of the oil, we think it clear that for taxing purposes this share of the proceeds received by the transferor is his income alone.

The broad and general view of local transactions which has been held proper in determining whose are the depletion deductions under the federal tax statutes must for consistency's sake be applied to questions of whose is the income. The holding in this case that the proceeds of oil paid to the transferors of the lease were taxable as income to the transferee taxpayers was erroneous.

The taxpayers had an interest in another transferred lease somewhat like that above discussed, but the claim for refund made no mention of that lease or the payments to its transferors but confined itself to the lease which we have discussed. The taxpayer cannot over objection enlarge his suit beyond the scope of his claim for refund. United States vs. Felt & Tarrant Co., 283 U. S. 269; Rock Island R. R. Co. vs. U. S., 254 U. S. 141; Turner vs. Alexander, 275 U. S. 228.

Error is also assigned that full costs were not allowed to the plaintiffs because they were only partially successful. This being a suit at law the court had no discretion to divide the costs, but the plaintiffs having recovered more than $500 were entitled to full costs. In Re Peterson, 253 U. S. 300, 318; Morris vs. First National Bank, 45 Fed. (2) 577; Harlan Coal Co. vs. North American Coal Corp., 35 Fed. (2) 211; Merritt vs. Merritt, 20 Fed. (2) 541. The rule was applied in a suit against a collector of internal revenue in West End Street Ry. Co. vs. Malley, Collector, 246 Fed. 625.

The exclusion from the taxpayers' income of the "oil payments" will necessitate an adjustment of their depletion allowance
181 and possibly other things. The adjustment can be best made in the trial court. The judgment is reversed and the cause remanded for further proceedings consistent herewith.

182 *Judgment*

Extract from the Minutes of December 18, 1936

No. 8172

J. J. PERKINS, ET AL. *vs.* W. A. THOMAS, COLLECTOR OF INTERNAL REVENUE

No. 8219

W. A. THOMAS, COLLECTOR OF INTERNAL REVENUE *vs.* J. J. PERKINS, ET AL.

This cause came on to be heard on the transcripts of the record from the District Court of the United States for the Northern District of Texas, and was argued by counsel;

On consideration whereof, It is now here ordered and adjudged by this Court, that the judgment of the said District Court in this cause be, and the same is hereby, reversed; and that this cause be, and it is

hereby, remanded to the said District Court for further proceedings consistent with the opinion of this Court.

184 *Clerk's certificate*

United States of America

United States Circuit Court of Appeals for the Fifth Circuit

I, Oakley F. Dodd, Clerk of the United States Circuit Court of Appeals for the Fifth Circuit, do hereby certify that the pages numbered from 174 to 184 next preceding this certificate contain full, true, and complete copies of all the pleadings, record entries, and proceedings, including the opinion of the United States Circuit Court of Appeals for the Fifth Circuit, in certain causes in said Court, numbered 8172 and 8219 respectively, wherein J. J. Perkins, et al., are appellants, and W. A. Thomas, Collector of Internal Revenue, is appellee, and W. A. Thomas, Collector of Internal Revenue, is cross-appellant, and J. J. Perkins, et al., are cross-appellees, as full, true, and complete as the originals of the same now remain in my office.

I further certify that the pages of the printed records numbered from 1 to 173 are identical with the printed records upon which said causes were heard and decided in the said Circuit Court of Appeals.

In testimony whereof, I hereunto subscribe my name and affix the seal of the said United States Circuit Court of Appeals, at my office in the City of New Orleans, Louisiana, in the Fifth Circuit, this 10th day of March A. D. 1937.

[SEAL]

OAKLEY F. DODD,
Clerk of the United States Circuit Court of Appeals, Fifth Circuit.

185 Supreme Court of the United States

Order allowing certiorari

Filed April 5, 1937

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Fifth Circuit is granted.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

(Endorsement on cover:) File No. 41, 364. U. S. Circuit Court of Appeals, Fifth Circuit. Term No. 824. W. A. Thomas, Collector of Internal Revenue, petitioner, vs. J. J. Perkins, et al. Petition for a writ of certiorari and exhibit thereto. Filed March 17, 1937. Term No. 824 O. T. 1936.

U. S. GOVERNMENT PRINTING OFFICE: 1937